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107TH CONGRESS, 1st Session } HOUSE OF REPRESENTATIVES { REPORT 107–251

ECONOMIC SECURITY AND RECOVERY ACT OF 2001

OCTOBER 17, 2001.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. THOMAS, from the Committee on Ways and Means, submitted the following

REPORT

together with

DISSENTING VIEWS

[To accompany H.R. 3090]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 3090) to provide tax incentives for economic recovery, having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

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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 "Economic Security and Recovery Act of 2001".

(b) REFERENCES TO INTERNAL REVENUE CODE OF 1986.—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) TABLE OF CONTENTS.—

Sec. 1. Short title; etc.

TITLE I—BUSINESS PROVISIONS

Sec. 101. Special depreciation allowance for certain property acquired after September 10, 2001, and before September 11, 2004.
Sec. 102. Temporary increase in expensing under section 179.
Sec. 103. Repeal of alternative minimum tax on corporations.
Sec. 104. Carryback of certain net operating losses allowed for 5 years.
Sec. 105. Recovery period for depreciation of certain leasehold improvements.

TITLE II—INDIVIDUAL PROVISIONS

Sec. 201. Acceleration of 25 percent individual income tax rate.
Sec. 202. Repeal of 5-year holding period requirement for reduced individual capital gains rates.
Sec. 203. Temporary increase in deduction for capital losses of taxpayers other than corporations.
Sec. 204. Temporary expansion of penalty-free retirement plan distributions for health insurance premiums of unemployed individuals.

TITLE III—EXTENSIONS OF CERTAIN EXPIRING PROVISIONS

Subtitle A—Two-Year Extensions

Sec. 301. Allowance of nonrefundable personal credits against regular and minimum tax liability.
Sec. 302. Credit for qualified electric vehicles.
Sec. 303. Credit for electricity produced from renewable resources.
Sec. 304. Work opportunity credit.
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Sec. 306. Deduction for clean-fuel vehicles and certain refueling property.
Sec. 307. Taxable income limit on percentage depletion for oil and natural gas produced from marginal properties.
Sec. 308. Qualified zone academy bonds.
Sec. 309. Cover over of tax on distilled spirits.
Sec. 310. Parity in the application of certain limits to mental health benefits.
Sec. 311. Delay in effective date of requirement for approved diesel or kerosene terminals.

Subtitle B—One-Year Extensions

Sec. 321. One-year extension of availability of medical savings accounts.

Subtitle C—Permanent Extensions

Sec. 331. Subpart F exemption for active financing.

Subtitle D—Other Provisions

Sec. 341. Excluded cancellation of indebtedness income of S corporation not to result in adjustment to basis of stock of shareholders.
Sec. 342. Limitation on use of nonaccrual experience method of accounting.

TITLE IV—SUPPLEMENTAL REBATE; OTHER PROVISIONS

Sec. 401. Supplemental rebate.
Sec. 402. Special Reed Act transfer in fiscal year 2002.

TITLE V—HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED

Sec. 501. Health care assistance for the unemployed.

TITLE I—BUSINESS PROVISIONS

SEC. 101. SPECIAL DEPRECIATION ALLOWANCE FOR CERTAIN PROPERTY ACQUIRED AFTER SEPTEMBER 10, 2001, AND BEFORE SEPTEMBER 11, 2004.

(a) IN GENERAL.—Section 168 (relating to accelerated cost recovery system) is amended by adding at the end the following new subsection:

"(k) SPECIAL ALLOWANCE FOR CERTAIN PROPERTY ACQUIRED AFTER SEPTEMBER 10, 2001, AND BEFORE SEPTEMBER 11, 2004.—

"(1) ADDITIONAL ALLOWANCE.—In the case of any qualified property—

"(A) the depreciation deduction provided by section 167(a) for the taxable year in which such property is placed in service shall include an allowance equal to 30 percent of the adjusted basis of the qualified property, and

"(B) the adjusted basis of the qualified property shall be reduced by the amount of such deduction before computing the amount otherwise allowable as a depreciation deduction under this chapter for such taxable year and any subsequent taxable year.

"(2) QUALIFIED PROPERTY.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'qualified property' means property—

"(i)(I) to which this section applies which has a recovery period of 20 years or less or which is water utility property, or

"(II) which is computer software (as defined in section 167(f)(1)(B)) for which a deduction is allowable under section 167(a) without regard to this subsection,

"(ii) the original use of which commences with the taxpayer after September 10, 2001,

"(iii) which is—

"(I) acquired by the taxpayer after September 10, 2001, and before September 11, 2004, but only if no written binding contract for the acquisition was in effect before September 11, 2001, or

"(II) acquired by the taxpayer pursuant to a written binding contract which was entered into after September 10, 2001, and before September 11, 2004, and

"(iv) which is placed in service by the taxpayer before January 1, 2005.

"(B) EXCEPTIONS.—

"(i) ALTERNATIVE DEPRECIATION PROPERTY.—The term 'qualified property' shall not include any property to which the alternative depreciation system under subsection (g) applies, determined—

"(I) without regard to paragraph (7) of subsection (g) (relating to election to have system apply), and

"(II) after application of section 280F(b) (relating to listed property with limited business use).

"(ii) ELECTION OUT.—If a taxpayer makes an election under this clause with respect to any class of property for any taxable year, this subsection shall not apply to all property in such class placed in service during such taxable year.

"(iii) REPAIRED OR RECONSTRUCTED PROPERTY.—Except as otherwise provided in regulations, the term 'qualified property' shall not include any repaired or reconstructed property.

"(iv) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY.—The term 'qualified property' shall not include any qualified leasehold improvement property (as defined in section 168(e)(6)).

"(C) SPECIAL RULES RELATING TO ORIGINAL USE.—

"(i) SELF-CONSTRUCTED PROPERTY.—In the case of a taxpayer manufacturing, constructing, or producing property for the taxpayer's own use, the requirements of clause (iii) of subparagraph (A) shall be treated as met if the taxpayer begins manufacturing, constructing, or producing the property after September 10, 2001, and before September 11, 2004.

"(ii) SALE-LEASEBACKS.—For purposes of subparagraph (A)(ii), if property—

"(I) is originally placed in service after September 10, 2001, by a person, and sold and leased back by such person within 3 months after the date such property was originally placed in service,

such property shall be treated as originally placed in service not earlier than the date on which such property is used under the leaseback referred to in subclause (II).

"(D) COORDINATION WITH SECTION 280F.—For purposes of section 280F—

"(i) AUTOMOBILES.—In the case of a passenger automobile (as defined in section 280F(d)(5)) which is qualified property, the Secretary shall increase the limitation under section 280F(a)(1)(A)(i) by $4,600.

"(ii) LISTED PROPERTY.—The deduction allowable under paragraph (1) shall be taken into account in computing any recapture amount under section 280F(b)(2)."

(b) ALLOWANCE AGAINST ALTERNATIVE MINIMUM TAX.—

(1) IN GENERAL.—Section 56(a)(1)(A) (relating to depreciation adjustment for alternative minimum tax) is amended by adding at the end the following new clause:

"(iii) ADDITIONAL ALLOWANCE FOR CERTAIN PROPERTY ACQUIRED AFTER SEPTEMBER 10, 2001, AND BEFORE SEPTEMBER 11, 2004.—The deduction under section 168(k) shall be allowed."

(2) CONFORMING AMENDMENT.—Clause (i) of section 56(a)(1)(A) is amended by striking "clause (ii)" both places it appears and inserting "clauses (ii) and (iii)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to property placed in service after September 10, 2001, in taxable years ending after such date.

SEC. 102. TEMPORARY INCREASE IN EXPENSING UNDER SECTION 179.

(a) IN GENERAL.—The table contained in section 179(b)(1) (relating to dollar limitation) is amended to read as follows:

"If the taxable year begins in:	The applicable amount is:
2001	$24,000
2002 or 2003	$35,000
2004 or thereafter	$25,000."

(b) TEMPORARY INCREASE IN AMOUNT OF PROPERTY TRIGGERING PHASEOUT OF MAXIMUM BENEFIT.—Paragraph (2) of section 179(b) is amended by inserting before the period "($325,000 in the case of taxable years beginning during 2002 or 2003)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2001.

SEC. 103. REPEAL OF ALTERNATIVE MINIMUM TAX ON CORPORATIONS.

(a) IN GENERAL.—So much of section 55 as precedes subsection (b)(2) is amended to read as follows:

"SEC. 55. ALTERNATIVE MINIMUM TAX FOR TAXPAYERS OTHER THAN CORPORATIONS.

"(a) IN GENERAL.—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, clause (i) shall be applied by substituting '$87,500' for '$175,000' each place it appears. For purposes of the preceding sentence, marital status shall be determined under section 7703."

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 55(b) is amended by striking "paragraph (1)(A)(i)" and inserting "paragraph (1)(A)".

(2) Paragraph (1) of section 55(c) is amended by striking ", the section 936 credit allowable under section 27(b), and the Puerto Rico economic activity credit under section 30A".

(3)(A) Paragraph (1) of section 55(d) is amended by—

(i) by striking "FOR TAXPAYERS OTHER THAN CORPORATIONS" in the heading, and

(ii) by striking "In the case of a taxpayer other than a corporation, the" and inserting "The".

(B) Section 55(d) is amended by striking paragraph (2) and by redesignating paragraph (3) as paragraph (2).

(C) Subparagraph (A) of section 55(d)(2), as so redesignated is amended by striking "or (2)".

(4) Section 55 is amended by striking subsection (e).

(5)(A) The designation and heading for subsection (a) of section 56 is amended to read as follows:

"(a) GENERAL RULES.—".

(B) Paragraph (1) of section 56(a) is amended by striking subparagraph (D).

(C) Paragraph (6) of section 56(a) is amended—

(i) by striking "paragraph (2) or subsection (b)(2)" and inserting "paragraph (2) or (9)", and

(ii) by striking "or (5), or subsection (b)(2)" and inserting "(5), or (9)".

(6)(A) Subsection (b) of section 56 is amended by striking so much of such subsection as precedes paragraph (1) and by redesignating paragraphs (1), (2), and (3) as paragraphs (8), (9), and (10), respectively, of subsection (a).

(B) Paragraph (9) of section 56(a), as so redesignated, is amended by striking subparagraph (C) and by redesignating subparagraph (D) as subparagraph (C).

(7) Section 56 is amended by striking subsections (c) and (g) and by redesignating subsections (d) and (e) as subsections (b) and (c), respectively.

(8) Subparagraph (E) of section 57(a)(2) is amended—

(A) by striking "FOR INDEPENDENT PRODUCERS" in the heading, and

(B) by striking clause (i) and inserting the following new clause:

"(i) IN GENERAL.—This paragraph shall not apply to any taxable year beginning after December 31, 1992."

(9) Subsection (a) of section 58 is amended by striking paragraph (3) and by redesignating paragraph (4) as paragraph (3).

(10)(A) Section 59 is amended by striking subsections (b) and (f) and by redesignating subsections (c), (d), (e), (g), (h), (i), and (j) as subsections (b), (c), (d), (e), (f), (g), and (h), respectively.

(B) Paragraph (2) of section 59(d), as so redesignated, is amended by striking "(determined without regard to section 291)".

(C) Sections 173(b), 174(f)(2), 263(c), 263A(c)(6), 616(e), 617(i), and 1016(a)(20) are each amended by striking "59(e)" each place it appears and inserting "59(d)".

(11) Subsection (d) of section 11 is amended by striking "the taxes imposed by subsection (a) and section 55" and inserting "the tax imposed by subsection (a)".

(12) Section 12 is amended by striking paragraph (7).

(13) Paragraph (6) of section 29(b) is amended to read as follows:

"(6) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and section 27. In the case of a taxpayer other than a corporation, such excess shall be further reduced (but not below zero) by the tentative minimum tax for the taxable year."

(14) Paragraph (3) of section 30(b) is amended to read as follows:

"(3) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and sections 27 and 29. In the case of a taxpayer other than a corporation, such excess shall be further reduced (but not below zero) by the tentative minimum tax for the taxable year."

(15)(A) Paragraph (1) of section 38(c) is amended to read as follows:

"(1) IN GENERAL.—

"(A) CORPORATIONS.—In the case of a corporation, the credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer's net income tax over 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000.

"(B) TAXPAYERS OTHER THAN CORPORATIONS.—In the case of a taxpayer other than a corporation, the credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer's net income tax over the greater of—

"(i) the tentative minimum tax for the taxable year, or

"(ii) 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000.

"(C) DEFINITIONS.—For purposes of this paragraph—

"(i) the term 'net income tax' means the sum of the regular tax liability and the tax imposed by section 55, reduced by the credits allowable under subparts A and B of this part, and

"(ii) the term 'net regular tax liability' means the regular tax liability reduced by the sum of the credits allowable under subparts A and B of this part."

(B) Clause (ii) of section 38(c)(2)(A) is amended to read as follows:

"(ii) for purposes of applying paragraph (1) to such credit—

"(I) the applicable limitation under paragraph (1) (as modified by subclause (II) in the case of a taxpayer other than a corporation) shall be reduced by the credit allowed under subsection (a) for the taxable year (other than the empowerment zone employment credit), and

"(II) in the case of a taxpayer other than a corporation, 75 percent of the tentative minimum tax shall be substituted for the tentative minimum tax under subparagraph (B)(i) thereof."

(C) Paragraph (3) of section 38(c) is amended by striking "subparagraph (B) of" each place it appears.

(16)(A) Subclause (I) of section 53(d)(1)(B)(ii) is amended by striking "subsection (b)(1)" and inserting "subsection (a)(8)".

(B) Clause (iv) of section 53(d)(1)(B) is hereby repealed.

(17)(A) Part VII of subchapter A of chapter 1 is hereby repealed.

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

(C) Paragraph (2) of section 26(b) is amended by striking subparagraph (B) and by redesignating the succeeding subparagraphs accordingly.

(D) Subsection (c) of section 30A is amended by striking paragraph (1) and redesignating the succeeding paragraphs accordingly.

(E) Subsection (a) of section 164 is amended by striking paragraph (5).

(F) Subsection (a) of section 275 is amended by striking "Paragraph (1) shall not apply to the tax imposed by section 59A."

(G) Paragraph (1) of section 882(a) is amended by striking "59A,".

(H) Paragraph (3) of section 936(a) is amended by striking subparagraph (A) and redesignating the succeeding subparagraphs accordingly.

(I) Subsection (a) of section 1561 is amended by adding "and" at the end of paragraph (2), by striking ", and" at the end of paragraph (3) and inserting a period, and by striking paragraph (4).

(J) Subparagraph (A) of section 6425(c)(1) is amended by adding "plus" at the end of clause (i), by striking "plus" at the end of clause (ii) and inserting "over", and by striking clause (iii).

(18) Section 382(l) (relating to limitation on net operating loss carryforwards and certain built-in losses following ownership change) is amended by striking paragraph (7) and by redesignating paragraph (8) as paragraph (7).

(19) Paragraph (2) of section 815(c) (relating to distributions to shareholders from pre-1984 policyholders surplus account) is amended by striking the last sentence.

(20) Section 847 (relating to special estimated tax payments) is amended—

(A) in paragraph (9), by striking the last sentence; and

(B) in paragraph (10), by inserting "and" at the end of subparagraph (A) and by striking subparagraph (B) and redesignating subparagraph (C) as subparagraph (B).

(21) Section 848 (relating to capitalization of certain policy acquisition expenses) is amended by striking subsection (i) and by redesignating subsection (j) as subsection (i).

(22) Paragraph (1) of section 882(a) (relating to tax on income of foreign corporations connected with United States business) is amended by striking "55,".

(23) Paragraph (1) of section 962(a) (relating to election by individuals to be subject to tax at corporate rates) is amended by striking "sections 11 and 55" and inserting "section 11".

(24) Subsection (a) of section 1561 (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) is amended by striking the last sentence.

(25) Subparagraph (A) of section 6425(c)(1) (defining income tax liability), as amended by paragraph (17) is amended to read as follows:

"(A) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever is applicable, over".

(26)(A) Paragraph (2) of section 6655(e) is amended—

(i) by striking ", alternative minimum taxable income, and modified alternative minimum taxable income" each place it appears in subparagraphs (A) and (B)(i), and

(ii) by striking clause (iii) of subparagraph (B).

(B) Subparagraph (A) of section 6655(g)(1) (relating to failure by corporation to pay estimated income tax), is amended to read as follows:

"(A) the sum of—

"(i) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever applies, plus

"(ii) the tax imposed by section 887, over".

(27) The table of sections for part VI of subchapter A of chapter 1 is amended by striking the item relating to section 55 and inserting the following new item:

"Sec. 55. Alternative minimum tax for taxpayers other than corporations."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2000.

(d) REFUND OF UNUSED MINIMUM TAX CREDIT.—

(1) IN GENERAL.—In the case of a corporation—

(A) section 53(c) of the Internal Revenue Code of 1986 shall not apply to such corporation's first taxable year beginning after December 31, 2000, and

(B) for purposes of such Code (other than section 53 of such Code), the credit allowed by section 53 of such Code for such first taxable year shall be treated as if it were allowed by subpart C of part IV of subchapter A of chapter 1 of such Code (relating to refundable credits).

(2) SPECIAL RULES RELATING TO CARRYBACKS.—In the case of a carryback of a corporation from a taxable year beginning after December 31, 2000, to a taxable year beginning before January 1, 2001—

(A) the tax imposed by section 55 of such Code shall not be increased or decreased by reason of such a carryback,

(B) tentative minimum tax shall not be increased or decreased by reason of such a carryback for purposes of determining the amount of any credit other than the credit allowed by section 38, and

(C) the amount of such a carryback which is taken into account in determining tentative minimum tax for purposes of section 38(c) shall be the amount of such carryback which is taken into account in determining regular tax liability.

SEC. 104. CARRYBACK OF CERTAIN NET OPERATING LOSSES ALLOWED FOR 5 YEARS.

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

"(H) In the case of a taxpayer which has a net operating loss for any taxable year ending after September 10, 2001, and before September 11, 2004, subparagraph (A)(i) shall be applied by substituting '5' for '2' and subparagraph (F) shall not apply.".

(b) ELECTION TO DISREGARD 5-YEAR CARRYBACK.—Section 172 (relating to net operating loss deduction) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) ELECTION TO DISREGARD 5-YEAR CARRYBACK FOR CERTAIN NET OPERATING LOSSES.—Any taxpayer entitled to a 5-year carryback under subsection (b)(1)(H) from any loss year may elect to have the carryback period with respect to such loss year determined without regard to subsection (b)(1)(H). 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. Such election, once made for any taxable year, shall be irrevocable for such taxable year.".

(c) TEMPORARY SUSPENSION OF 90 PERCENT LIMIT ON CERTAIN NOL CARRYBACKS.—Subparagraph (A) of section 56(b)(1) (relating to general rule defining alternative tax net operating loss deduction), as amended by section 103, is amended to read as follows:

"(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 attributable to carrybacks described in clause (ii)(I)), or

"(II) 90 percent of alternate minimum taxable income determined without regard to such deduction, plus

"(ii) the lesser of—

"(I) the amount of such deduction attributable to carrybacks of net operating losses for taxable years ending after September 10, 2001, and before September 11, 2004, or

"(II) alternate minimum taxable income determined without regard to such deduction reduced by the amount determined under clause (i), and".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to net operating losses for taxable years ending after September 10, 2001.

SEC. 105. RECOVERY PERIOD FOR DEPRECIATION OF CERTAIN LEASEHOLD IMPROVEMENTS.

(a) 15-YEAR RECOVERY PERIOD.—Subparagraph (E) of section 168(e)(3) (relating to 15-year property) is amended by striking "and" at the end of clause (ii), by striking the period at the end of clause (iii) and inserting ", and", and by adding at the end the following new clause:

"(iv) any qualified leasehold improvement property.".

(b) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY.—Subsection (e) of section 168 is amended by adding at the end the following new paragraph:

"(6) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY.—

"(A) IN GENERAL.—The term 'qualified leasehold improvement property' means any improvement to an interior portion of a building which is nonresidential real property if—

"(i) such improvement is made under or pursuant to a lease (as defined in subsection (h)(7))—

"(I) by the lessee (or any sublessee) of such portion, or

"(II) by the lessor of such portion,

"(ii) such portion is to be occupied exclusively by the lessee (or any sublessee) of such portion, and

"(iii) such improvement is placed in service more than 3 years after the date the building was first placed in service.

"(B) CERTAIN IMPROVEMENTS NOT INCLUDED.—Such term shall not include any improvement for which the expenditure is attributable to—

"(i) the enlargement of the building,

"(ii) any elevator or escalator,

"(iii) any structural component benefiting a common area, and

"(iv) the internal structural framework of the building.

"(C) DEFINITIONS AND SPECIAL RULES.—For purposes of this paragraph—

"(i) COMMITMENT TO LEASE TREATED AS LEASE.—A commitment to enter into a lease shall be treated as a lease, and the parties to such commitment shall be treated as lessor and lessee, respectively.

"(ii) RELATED PERSONS.—A lease between related persons shall not be considered a lease. For purposes of the preceding sentence, the term 'related persons' means—

"(I) members of an affiliated group (as defined in section 1504), and

"(II) persons having a relationship described in subsection (b) of section 267; except that, for purposes of this clause, the phrase '80 percent or more' shall be substituted for the phrase 'more than 50 percent' each place it appears in such subsection.

"(D) IMPROVEMENTS MADE BY LESSOR.—

"(i) IN GENERAL.—In the case of an improvement made by the person who was the lessor of such improvement when such improvement was placed in service, such improvement shall be qualified leasehold improvement property (if at all) only so long as such improvement is held by such person.

"(ii) EXCEPTION FOR CHANGES IN FORM OF BUSINESS.—Property shall not cease to be qualified leasehold improvement property under clause (i) by reason of—

"(I) death,

"(II) a transaction to which section 381(a) applies, or

"(III) a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as qualified leasehold improvement property and the taxpayer retains a substantial interest in such trade or business."

(c) REQUIREMENT TO USE STRAIGHT LINE METHOD.—Paragraph (3) of section 168(b) is amended by adding at the end the following new subparagraph:

"(G) Qualified leasehold improvement property described in subsection (e)(6).".

(d) ALTERNATIVE SYSTEM.—The table contained in section 168(g)(3)(B) is amended by adding at the end the following new item:

"(E)(iv) ..... 15".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to qualified leasehold improvement property placed in service after September 10, 2001.

TITLE II—INDIVIDUAL PROVISIONS

SEC. 201. ACCELERATION OF 25 PERCENT INDIVIDUAL INCOME TAX RATE.

(a) IN GENERAL.—The table contained in paragraph (2) of section 1(i) (relating to reductions in rates after June 30, 2001) is amended—

(1) by striking "27.0%" and inserting "25.0%", and

(2) by striking "26.0%" and inserting "25.0%".

(b) REDUCTION NOT TO INCREASE MINIMUM TAX.—

(1) Subparagraph (A) of section 55(d)(1) is amended by striking "($49,000 in the case of taxable years beginning in 2001, 2002, 2003, and 2004)" and inserting "($49,000 in the case of taxable years beginning in 2001, $52,200 in the case of taxable years beginning in 2002 or 2003, and $50,700 in the case of taxable years beginning in 2004)".

(2) Subparagraph (B) of section 55(d)(1) is amended by striking "($35,750 in the case of taxable years beginning in 2001, 2002, 2003, and 2004)" and inserting "($35,750 in the case of taxable years beginning in 2001, $37,350 in the case of taxable years beginning in 2002 or 2003, and $36,600 in the case of taxable years beginning in 2004)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2001.

(d) SECTION 15 NOT TO APPLY.—No amendment made by this section shall be treated as a change in a rate of tax for purposes of section 15 of the Internal Revenue Code of 1986.

SEC. 202. REPEAL OF 5-YEAR HOLDING PERIOD REQUIREMENT FOR REDUCED INDIVIDUAL CAPITAL GAINS RATES.

(a) IN GENERAL.—

(1) Sections 1(h)(1)(B) and 55(b)(3)(B) are each amended by striking "10 percent" and inserting "8 percent".

(2) The following sections are each amended by striking "20 percent" and inserting "18 percent":

(A) Section 1(h)(1)(C).

(B) Section 55(b)(3)(C).

(C) Section 1445(e)(1).

(D) The second sentence of section 7518(g)(6)(A).

(E) The second sentence of section 607(h)(6)(A) of the Merchant Marine Act, 1936.

(b) CONFORMING AMENDMENTS.—

(1) Subsection (e) of section 311 of the Taxpayer Relief Act of 1997 is repealed.

(2) Section 1(h) is amended—

(A) by striking paragraphs (2) and (9),

(B) by redesignating paragraphs (3) through (8) as paragraphs (2) through (7), respectively, and

(C) by redesignating paragraphs (10), (11), and (12) as paragraphs (8), (9), and (10), respectively.

(3) Paragraph (3) of section 55(b) is amended by striking "In the case of taxable years beginning after December 31, 2000, rules similar to the rules of section 1(h)(2) shall apply for purposes of subparagraphs (B) and (C).".

(4) Paragraph (7) of section 57(a) is amended by striking the last sentence and by striking "42 percent" and inserting "28 percent".

(c) TRANSITIONAL RULES FOR TAXABLE YEARS WHICH INCLUDE OCTOBER 12, 2001.—For purposes of applying section 1(h) of the Internal Revenue Code of 1986 in the case of a taxable year which includes October 12, 2001—

(1) The amount of tax determined under subparagraph (B) of section 1(h)(1) of such Code shall be the sum of—

(A) 8 percent of the lesser of—

(i) the sum of—

(I) the net capital gain taking into account only gain or loss properly taken into account for the portion of the taxable year on or after October 12, (determined without regard to collectibles gain or

loss, gain described in section (1)(h)(6)(A)(i) of such Code, and section 1202 gain), and

(II) the qualified 5-year gain (as defined in section 1(h)(9) of the Internal Revenue Code of 1986, as in effect on the day before the date of the enactment of this Act) properly taken into account for the portion of the taxable year before October 12, 2001, or

(ii) the amount on which a tax is determined under such subparagraph (without regard to this subsection), plus

(B) 10 percent of the excess (if any) of—

(i) the amount on which a tax is determined under such subparagraph (without regard to this subsection), over

(ii) the amount on which a tax is determined under subparagraph (A).

(2) The amount of tax determined under subparagraph (C) of section (1)(h)(1) of such Code shall be the sum of—

(A) 18 percent of the lesser of—

(i) the excess (if any) of the amount of net capital gain determined under subparagraph (A)(i)(I) of paragraph (1) of this subsection over the amount on which a tax is determined under subparagraph (A) of paragraph (1) of this subsection, or

(ii) the amount on which a tax is determined under such subparagraph (C) (without regard to this subsection), plus

(B) 20 percent of the excess (if any) of—

(i) the amount on which a tax is determined under such subparagraph (C) (without regard to this subsection), over

(ii) the amount on which a tax is determined under subparagraph (A) of this paragraph.

(3) For purposes of applying section 55(b)(3) of such Code, rules similar to the rules of paragraphs (1) and (2) of this subsection shall apply.

(4) In applying this subsection with respect to any pass-thru entity, the determination of when gains and loss are properly taken into account shall be made at the entity level.

(5) Terms used in this subsection which are also used in section 1(h) of such Code shall have the respective meanings that such terms have in such section.

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided by this subsection, the amendments made by this section shall apply to taxable years ending on or after October 12, 2001.

(2) WITHHOLDING.—The amendment made by subsection (a)(2)(C) shall apply to amounts paid after the date of the enactment of this Act.

(3) ELECTION TO RECOGNIZE GAIN ON ASSESTS HELD ON JANUARY 1, 2001.—The repeal made by subsection (b)(1) shall take effect as if included in section 311 of the Taxpayer Relief Act of 1997, and the Internal Revenue Code of 1986 shall be applied and administered as if subsection (e) of such section 311 had never been enacted.

(4) SMALL BUSINESS STOCK.—The amendments made by subsection (b)(4) shall apply to dispositions on or after October 12, 2001.

SEC. 203. TEMPORARY INCREASE IN DEDUCTION FOR CAPITAL LOSSES OF TAXPAYERS OTHER THAN CORPORATIONS.

(a) IN GENERAL.—Subsection (b) of section 1211 (relating to limitation on capital losses for taxpayers other than corporations) is amended by adding at the end the following flush sentence:

"Paragraph (1) shall be applied by substituting '$4,000' for '$3,000' and '$2,000' for '$1,500' in the case of taxable years beginning in 2001, and by substituting '$5,000' for '$3,000' and '$2,500' for '$1,500' in the case of taxable years beginning in 2002.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2000.

SEC. 204. TEMPORARY EXPANSION OF PENALTY-FREE RETIREMENT PLAN DISTRIBUTIONS FOR HEALTH INSURANCE PREMIUMS OF UNEMPLOYED INDIVIDUALS.

(a) IN GENERAL.—Subparagraph (D) of section 72(t)(2) is amended by adding at the end the following new clause:

"(iv) SPECIAL RULES FOR INDIVIDUALS RECEIVING UNEMPLOYMENT COMPENSATION AFTER SEPTEMBER 10, 2001, AND BEFORE JANUARY 1, 2003.—In the case of an individual who receives unemployment compensation for 4 consecutive weeks after September 10, 2001, and before January 1, 2003—

"(I) clause (i) shall apply to distributions from all qualified retirement plans (as defined in section 4974(c)), and

"(II) such 4 consecutive weeks shall be substituted for the 12 consecutive weeks referred to in subclause (I) of clause (i)."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to distributions after the date of the enactment of this Act.

TITLE III—EXTENSIONS OF CERTAIN EXPIRING PROVISIONS

Subtitle A—Two-Year Extensions

SEC. 301. ALLOWANCE OF NONREFUNDABLE PERSONAL CREDITS AGAINST REGULAR AND MINIMUM TAX LIABILITY.

(a) IN GENERAL.—Paragraph (2) of section 26(a) is amended—

(1) by striking "RULE FOR 2000 AND 2001.—" and inserting "RULE FOR 2000, 2001, 2002, AND 2003.—", and

(2) by striking "during 2000 or 2001," and inserting "during 2000, 2001, 2002, or 2003,".

(b) CONFORMING AMENDMENTS.—

(1) Section 904(h) is amended by striking "during 2000 or 2001" and inserting "during 2000, 2001, 2002, or 2003".

(2) The amendments made by sections 201(b), 202(f), and 618(f) of the Economic Growth and Tax Relief Reconciliation Act of 2001 shall not apply to taxable years beginning during 2002 and 2003.

(c) TECHNICAL CORRECTION.—Section 24(d)(1)(B) is amended by striking "amount of credit allowed by this section" and inserting "aggregate amount of credits allowed by this subpart".

(d) EFFECTIVE DATES.—

(1) The amendments made by subsections (a) and (b) shall apply to taxable years beginning after December 31, 2001.

(2) The amendment made by subsection (c) shall apply to taxable years beginning after December 31, 2000.

SEC. 302. CREDIT FOR QUALIFIED ELECTRIC VEHICLES.

(a) IN GENERAL.—Section 30 is amended—

(1) in subsection (b)(2)—

(A) by striking "December 31, 2001," and inserting "December 31, 2003,", and

(B) in subparagraphs (A), (B), and (C), by striking "2002", "2003", and "2004", respectively, and inserting "2004", "2005", and "2006", respectively, and

(2) in subsection (e), by striking "December 31, 2004" and inserting "December 31, 2006".

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (C) of section 280F(a)(1) is amended by adding at the end the following new clause

"(iii) APPLICATION OF SUBPARAGRAPH.—This subparagraph shall apply to property placed in service after August 5, 1997, and before January 1, 2007.".

(2) Subsection (b) of section 971 of the Taxpayer Relief Act of 1997 is amended by striking "and before January 1, 2005".

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

SEC. 303. CREDIT FOR ELECTRICITY PRODUCED FROM RENEWABLE RESOURCES.

(a) IN GENERAL.—Subparagraphs (A), (B), and (C) of section 45(c)(3) are each amended by striking "2002" and inserting "2004".

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

SEC. 304. WORK OPPORTUNITY CREDIT.

(a) IN GENERAL.—Subparagraph (B) of section 51(c)(4) is amended by striking "2001" and inserting "2003".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to individuals who begin work for the employer after December 31, 2001.

SEC. 305. WELFARE-TO-WORK CREDIT.

(a) IN GENERAL.—Subsection (f) of section 51A is amended by striking "2001" and inserting "2003".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to individuals who begin work for the employer after December 31, 2001.

SEC. 306. DEDUCTION FOR CLEAN-FUEL VEHICLES AND CERTAIN REFUELING PROPERTY.

(a) IN GENERAL.—Section 179A is amended—

(1) in subsection (b)(1)(B)—

(A) by striking "December 31, 2001," and inserting "December 31, 2003,", and

(B) in clauses (i), (ii), and (iii), by striking "2002", "2003", and "2004", respectively, and inserting "2004", "2005", and "2006", respectively, and

(2) in subsection (f), by striking "December 31, 2004" and inserting "December 31, 2006".

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

SEC. 307. TAXABLE INCOME LIMIT ON PERCENTAGE DEPLETION FOR OIL AND NATURAL GAS PRODUCED FROM MARGINAL PROPERTIES.

(a) IN GENERAL.—Subparagraph (H) of section 613A(c)(6) is amended by striking "2002" and inserting "2004".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2001.

SEC. 308. QUALIFIED ZONE ACADEMY BONDS.

(a) IN GENERAL.—Paragraph (1) of section 1397E(e) is amended by striking "2000, and 2001" and inserting "2000, 2001, 2002, and 2003".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

SEC. 309. COVER OVER OF TAX ON DISTILLED SPIRITS.

(a) IN GENERAL.—Paragraph (1) of section 7652(f) is amended by striking "January 1, 2002" and inserting "January 1, 2004".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

SEC. 310. PARITY IN THE APPLICATION OF CERTAIN LIMITS TO MENTAL HEALTH BENEFITS.

(a) IN GENERAL.—Subsection (f) of section 9812 is amended by striking "2001" and inserting "2003".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to plan years beginning after December 31, 2001.

SEC. 311. DELAY IN EFFECTIVE DATE OF REQUIREMENT FOR APPROVED DIESEL OR KEROSENE TERMINALS.

Paragraph (2) of section 1032(f) of the Taxpayer Relief Act of 1997 (Public Law 105–34) is amended by striking "January 1, 2002" and inserting "January 1, 2004".

Subtitle B—One-Year Extensions

SEC. 321. ONE-YEAR EXTENSION OF AVAILABILITY OF MEDICAL SAVINGS ACCOUNTS.

(a) IN GENERAL.—Paragraphs (2) and (3)(B) of section 220(i) (defining cut-off year) are each amended by striking "2002" each place it appears and inserting "2003".

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 220(j) is amended by striking "1998, 1999, or 2001" each place it appears and inserting "1998, 1999, 2001, or 2002".

(2) Subparagraph (A) of section 220(j)(4) is amended by striking "and 2001" and inserting "2001, and 2002".

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

Subtitle C—Permanent Extensions

SEC. 331. SUBPART F EXEMPTION FOR ACTIVE FINANCING.

(a) IN GENERAL.—

(1) Section 953(e)(10) is amended—

(A) by striking ", and before January 1, 2002,", and

(B) by striking the second sentence.

(2) Section 954(h)(9) is amended by striking ", and before January 1, 2002,".

(b) LIFE INSURANCE AND ANNUITY CONTRACTS.—

(1) IN GENERAL.—Subparagraph (B) of section 954(i)(4) is amended to read as follows:

"(B) LIFE INSURANCE AND ANNUITY CONTRACTS.—

"(i) IN GENERAL.—Except as provided in clause (ii), the amount of the reserve of a qualifying insurance company or qualifying insurance company branch for any life insurance or annuity contract shall be equal to the greater of—

"(I) the net surrender value of such contract (as defined in section 807(e)(1)(A)), or

"(II) the reserve determined under paragraph (5).

"(ii) RULING REQUEST.—The amount of the reserve under clause (i) shall be the foreign statement reserve for the contract (less any catastrophe, deficiency, equalization, or similar reserves), if, pursuant to a ruling request submitted by the taxpayer, the Secretary determines that the factors taken into account in determining the foreign statement reserve provide an appropriate means of measuring income.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2001.

Subtitle D—Other Provisions

SEC. 341. EXCLUDED CANCELLATION OF INDEBTEDNESS INCOME OF S CORPORATION NOT TO RESULT IN ADJUSTMENT TO BASIS OF STOCK OF SHAREHOLDERS.

(a) IN GENERAL.—Subparagraph (A) of section 108(d)(7) (relating to certain provisions to be applied at corporate level) is amended by inserting before the period ", including by not taking into account under section 1366(a) any amount excluded under subsection (a) of this section".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to discharges of indebtedness after October 11, 2001, in taxable years ending after such date.

SEC. 342. LIMITATION ON USE OF NONACCRUAL EXPERIENCE METHOD OF ACCOUNTING.

(a) IN GENERAL.—Paragraph (5) of section 448(d) is amended to read as follows:

"(5) SPECIAL RULE FOR CERTAIN SERVICES.—

"(A) IN GENERAL.—In the case of any person using an accrual method of accounting with respect to amounts to be received for the performance of services by such person, such person shall not be required to accrue any portion of such amounts which (on the basis of such person's experience) will not be collected if—

"(i) such services are in fields referred to in paragraph (2)(A), or

"(ii) such person meets the gross receipts test of subsection (c) for all prior taxable years.

"(B) EXCEPTION.—This paragraph shall not apply to any amount if interest is required to be paid on such amount or there is any penalty for failure to timely pay such amount.

"(C) REGULATIONS.—The Secretary shall prescribe regulations to permit taxpayers to determine amounts referred to in subparagraph (A) using computations or formulas which, based on experience, accurately reflect the amount of income that will not be collected by such person. A taxpayer may adopt, or request consent of the Secretary to change to, a computation or formula that clearly reflects the taxpayer's experience. A request under the preceding sentence shall be approved only if such computation or formula clearly reflects the taxpayer's experience.".

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

(2) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer required by the amendments made by this section to change its method of accounting for its first taxable year ending after the date of the enactment of this Act—

(A) such change shall be treated as initiated by the taxpayer,

(B) such change shall be treated as made with the consent of the Secretary of the Treasury, and

(C) the net amount of the adjustments required to be taken into account by the taxpayer under section 481 of the Internal Revenue Code of 1986 shall be taken into account over a period of 4 years (or if less, the number of taxable years that the taxpayer used the method permitted under section 448(d)(5) of such Code as in effect before the date of the enactment of this Act) beginning with such first taxable year.

TITLE IV—SUPPLEMENTAL REBATE; OTHER PROVISIONS

SEC. 401. SUPPLEMENTAL REBATE.

(a) IN GENERAL.—Section 6428 (relating to acceleration of 10 percent income tax rate bracket benefit for 2001) is amended by adding at the end the following new subsection:

"(f) SUPPLEMENTAL REBATE.—

"(1) IN GENERAL.—Each individual who was an eligible individual for such individual's first taxable year beginning in 2000 and who, before October 16, 2001, filed a return of tax imposed by subtitle A for such taxable year shall be treated as having made a payment against the tax imposed by chapter 1 for such first taxable year in an amount equal to the supplemental refund amount for such taxable year.

"(2) SUPPLEMENTAL REFUND AMOUNT.—For purposes of this subsection, the supplemental refund amount is an amount equal to the excess (if any) of—

"(A)(i) $600 in the case of taxpayers to whom section 1(a) applies,

"(ii) $500 in the case of taxpayers to whom section 1(b) applies, and

"(iii) $300 in the case of taxpayers to whom subsections (c) or (d) of section 1 applies, over

"(B) the taxpayer's advance refund amount under subsection (e).

"(3) TIMING OF PAYMENTS.—In the case of any overpayment attributable to this subsection, the Secretary shall, subject to the provisions of this title, refund or credit such overpayment as rapidly as possible.

"(4) NO INTEREST.—No interest shall be allowed on any overpayment attributable to this subsection."

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (A) of section 6428(d)(1) is amended by striking "subsection (e)" and inserting "subsections (e) and (f)".

(2) Subparagraph (B) of section 6428(d)(1) is amended by striking "subsection (e)" and inserting "subsection (e) or (f)".

(3) Paragraph (3) of section 6428(e) is amended by striking "December 31, 2001" and inserting "the date of the enactment of the Economic Security and Recovery Act of 2001".

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

SEC. 402. SPECIAL REED ACT TRANSFER IN FISCAL YEAR 2002.

(a) REPEAL OF CERTAIN PROVISIONS ADDED BY THE BALANCED BUDGET ACT OF 1997.—

(1) IN GENERAL.—The following provisions of section 903 of the Social Security Act (42 U.S.C. 1103) are repealed:

(A) Paragraph (3) of subsection (a).

(B) The last sentence of subsection (c)(2).

(2) SAVINGS PROVISION.—Any amounts transferred before the date of enactment of this Act under the provision repealed by paragraph (1)(A) shall remain subject to section 903 of the Social Security Act, as last in effect before such date of enactment.

(b) SPECIAL TRANSFER IN FISCAL YEAR 2002.—Section 903 of the Social Security Act is amended by adding at the end the following:

"Special Transfer in Fiscal Year 2002

"(d)(1) The Secretary of the Treasury shall transfer (as of the date determined under paragraph (5)(A)) from the Federal unemployment account to the account of each State in the Unemployment Trust Fund the amount determined with respect to such State under paragraph (2).

"(2) The amount to be transferred under this subsection to a State account shall (as determined by the Secretary of Labor and certified by such Secretary to the Secretary of the Treasury) be equal to—

"(A) the amount which would have been required to have been transferred under this section to such account at the beginning of fiscal year 2002 if section 402(a)(1) of the Economic Security and Recovery Act of 2001 had been enacted before the close of fiscal year 2001, minus

"(B) the amount which was in fact transferred under this section to such account at the beginning of fiscal year 2002.

"(3)(A) Except as provided in paragraph (4), amounts transferred to a State account pursuant to this subsection may be used only in the payment of cash benefits—

"(i) to individuals with respect to their unemployment, and

"(ii) which are allowable under subparagraph (B) or (C).

"(B)(i) At the option of the State, cash benefits under this paragraph may include amounts which shall be payable as regular or additional compensation for individuals eligible for regular compensation under the unemployment compensation law of such State.

"(ii) Any additional compensation under clause (i) may not be taken into account for purposes of any determination relating to the amount of any extended compensation for which an individual might be eligible.

"(C)(i) At the option of the State, cash benefits under this paragraph may include amounts which shall be payable to 1 or more categories of individuals not otherwise eligible for regular compensation under the unemployment compensation law of such State.

"(ii) The benefits paid under this subparagraph to any individual may not, for any period of unemployment, exceed the maximum amount of regular compensation authorized under the unemployment compensation law of such State for that same period, plus any additional benefits (described in subparagraph (B)(i)) which could have been paid with respect to that amount.

"(D) Amounts transferred to a State account under this subsection may be used in the payment of cash benefits to individuals only for weeks of unemployment—

"(i) beginning after the date of enactment of this subsection, and

"(ii) ending on or before March 11, 2003.

"(4) Amounts transferred to a State account under this subsection may be used for the administration of its unemployment compensation law and public employment offices (including in connection with benefits described in paragraph (3) and any recipients thereof), subject to the same conditions as set forth in subsection (c)(2) (excluding subparagraph (B) thereof, and deeming the reference to 'subsections (a) and (b)' in subparagraph (D) thereof to include this subsection).

"(5) Transfers under this subsection—

"(A) shall be made on such date as the Secretary of Labor (in consultation with the Secretary of the Treasury) shall determine, but in no event later than 10 days after the date of enactment of this subsection, and

"(B) may, notwithstanding any other provision of this subsection, be made only to the extent that they do not to exceed—

"(i) the balance in the Federal unemployment account as of the date determined under subparagraph (A), or

"(ii) the total amount that was transferred under this section to the Federal unemployment account at the beginning of fiscal year 2002,

whichever is less."

(c) LIMITATIONS ON TRANSFERS.—Section 903(b) of the Social Security Act shall apply to transfers under section 903(d) of such Act (as amended by this section). For purposes of the preceding sentence, such section 903(b) shall be deemed to be amended as follows:

(1) By substituting "the transfer date described in subsection (d)(5)(A)" for "October 1 of any fiscal year".

(2) By substituting "remain in the Federal unemployment account" for "be transferred to the Federal unemployment account as of the beginning of such October 1".

(3) By substituting "fiscal year 2002 (after the transfer date described in subsection (d)(5)(A))" for "the fiscal year beginning on such October 1".

(4) By substituting "under subsection (d)" for "as of October 1 of such fiscal year".

(5) By substituting "(as of the close of fiscal year 2002)" for "(as of the close of such fiscal year)".

(d) TECHNICAL AMENDMENTS.—(1) Sections 3304(a)(4)(B) and 3306(f)(2) of the Internal Revenue Code of 1986 are amended by inserting "or 903(d)(4)" before "of the Social Security Act".

(2) Section 303(a)(5) of the Social Security Act is amended in the second proviso by inserting "or 903(d)(4)" after "903(c)(2)".

(e) REGULATIONS.—The Secretary of Labor may prescribe any operating instructions or regulations necessary to carry out this section and the amendments made by this section.

TITLE V—HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED

SEC. 501. HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED.

Title XX of the Social Security Act (42 U.S.C. 1397–1397f) is amended by adding at the end the following:

"SEC. 2008. GRANTS FOR HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED.

"(a) FUNDING.—For purposes of section 2003, the amount specified in section 2003(c) for fiscal year 2002 is increased by $3,000,000,000.

"(b) USE OF FUNDS.—Notwithstanding any other provision of this title, to the extent that an amount paid to a State under section 2002 is attributable to funds made available by reason of subsection (a) of this section—

"(1) the State shall use the amount to assist an unemployed individual who is not eligible for Federal health coverage to purchase health care coverage for the individual or any member of the family of the individual who is not so eligible; and

"(2) the amount—

"(A) shall be used to supplement, not supplant, any other Federal, State, or local funds that are used for the provision of health care coverage; and

"(B) may not be included in determining the amount of non-Federal contributions required under any program.

"(c) DEFINITIONS.—In this section:

"(1) UNEMPLOYED INDIVIDUAL.—The term 'unemployed individual' means an individual who—

"(A) is without a job (determined in accordance with the criteria used by the Bureau of Labor Statistics of the Department of Labor in defining individuals as unemployed);

"(B) is seeking and available for work; and

"(C) has or had a benefit year (within the meaning of section 205 of the Federal-State Extended Unemployment Compensation Act of 1970) beginning on or after January 1, 2001.

"(2) FEDERAL HEALTH COVERAGE.—

"(A) IN GENERAL.—Subject to subparagraph (B), the term 'Federal health coverage' means coverage under any medical care program described in—

"(i) title XVIII, XIX, or XXI of this Act (other than under section 1928);

"(ii) chapter 55 of title 10, United States Code;

"(iii) chapter 17 of title 38, United States Code;

"(iv) chapter 89 of title 5, United States Code (other than coverage which is comparable to continuation coverage under section 4980B of the Internal Revenue Code of 1986); or

"(v) the Indian Health Care Improvement Act.

"(B) SPECIAL RULE.—Such term does not include coverage under a qualified long-term care insurance contract.".

I. SUMMARY AND BACKGROUND

A. PURPOSE AND SUMMARY

The bill, H.R. 3090, as amended (the "Economic Security and Recovery Act of 2001"), provides tax incentives for economic recovery.

The bill provides net tax reductions and outlays of over $159.4 billion over fiscal years 2002–2011. The bill will provide tax relief for businesses and individuals that will stimulate many sectors of the economy.

The bill allows an additional first-year depreciation deduction for certain qualified property and increases the maximum amount that may be deducted under section 179. The bill provides a 15-year life for leasehold improvements. The bill temporarily extends the general net operating loss carryback period to five years. The bill also repeals the corporate alternative minimum tax. The bill extends permanently the present-law temporary exceptions from subpart F foreign personal holding company income, foreign base company

services income, and insurance income for certain income that is derived in the active conduct of a banking, financing or similar business, or in the conduct of an insurance business.

The bill provides a rebate for certain individuals who filed a tax return for 2000. The bill accelerates the 25-percent individual income tax rate and increases the alternative minimum tax exemption amount for individuals. The bill also increases the deduction of capital losses of individuals that may offset ordinary income. The bill eliminates the 5-year holding period for reduced individual capital gains rates. The bill also expands the exception to the early withdrawal tax for IRA distributions used for health insurance for unemployed individuals.

The bill provides a two-year extension of provisions expiring in 2001, including: alternative minimum tax relief for individuals; the work opportunity tax credit; the welfare-to-work tax credit; the tax credit for production of electricity from wind, closed loop biomass, and poultry litter; suspension of taxable income limit on percentage depletion for marginal production; authority to issue qualified zone academy bonds; increased carryover payments to Puerto Rico and the Virgin Islands; suspension of the effective date of the diesel fuel and kerosene dying mandate; the deduction for qualified clean-fuel vehicle property and qualified clean-fuel vehicle refueling property; the credit for purchase of electric vehicles; and the tax on failures to comply with mental health parity requirements. The bill also extends the Archer MSA program for one year.

The bill limits the use of the non-accrual experience method of accounting. The bill also provides that income from the discharge of indebtedness of an S corporation that is excluded from the S corporation's income does not increase a shareholder's stock basis. These provisions provide revenue offsets for the economic stimulus provisions of the bill and also improve the operation of the Federal income tax system by closing loopholes and achieving a more accurate measurement of income in those situations affected by the provisions.

The bill repeals a provision of the 1997 Balanced Budget Act which limited distributions of surplus Federal unemployment trust funds to the States. Approximately $9 billion will be available to States. The bill increases by $3 billion, in fiscal year 2002 only, funding for the Social Services Block Grant Program to assist States in providing health care coverage for unemployed workers and their families who do not have health care coverage.

B. Background and Need for Legislation

The terrorist attacks of September 11, 2001 have affected the United States in numerous ways. In addition to the tremendous number of lives lost, the September 11, 2001 attacks have caused adverse effects to the U.S. economy. Thousands of Americans have lost jobs. Consumer confidence and investor confidence are low. The Committee believes that it is necessary to spur economic growth and job creation and help struggling business and unemployed workers. The provisions approved by the Committee will stimulate and strengthen the economy.

C. Legislative History

COMMITTEE ACTION

The Committee on Ways and Means marked up the provisions of the bill on October 12, 2001, and reported the provisions, as amended, on October 12, 2001, by a rollcall vote of 23 yeas and 14 nays, with a quorum present.

II. EXPLANATION OF THE BILL

TITLE I: BUSINESS PROVISIONS

A. Special Depreciation Allowance for Certain Property (Sec. 101 of the Bill and Sec. 168 and Sec. 280F of the Code)

PRESENT LAW

Depreciation deductions

A taxpayer is allowed to recover, through annual depreciation deductions, the cost of certain property used in a trade or business or for the production of income. The amount of the depreciation deduction allowed with respect to tangible property for a taxable year is determined under the modified accelerated cost recovery system ("MACRS"). Under MACRS, different types of property generally are assigned applicable recovery periods and depreciation methods. The recovery periods applicable to most tangible personal property (generally tangible property other than residential rental property and nonresidential real property) range from 3 to 25 years. The depreciation methods generally applicable to tangible personal property are the 200-percent and 150-percent declining balance methods, switching to the straight-line method for the taxable year in which the depreciation deduction would be maximized.

Section 280F limits the annual depreciation deductions with respect to passenger automobiles to specified dollar amounts, indexed for inflation.

Section 167(f)(1) provides that capitalized computer software costs, other than computer software to which section 197 applies, are recovered ratably over 36 months.

Expensing election

In lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $24,000 (for taxable years beginning in 2001 or 2002) of the cost of qualifying property placed in service for the taxable year (sec. 179). This amount is increased to $25,000 for taxable years beginning in 2003 and thereafter. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $24,000 ($25,000 for taxable years beginning in 2003 and thereafter) amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $200,000. In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income for a taxable year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation

may be carried forward to succeeding taxable years (subject to similar limitations). No general business credit under section 38 shall be allowed with respect to any amount for which a deduction is allowed under section 179.

REASONS FOR CHANGE

The Committee believes that allowing additional first-year depreciation will accelerate purchases of equipment, promote capital investment, modernization, and growth, and will help to spur an economic recovery.

EXPLANATION OF PROVISION

The provision allows an additional first-year depreciation deduction equal to 30 percent of the adjusted basis of certain qualified property that is placed in service before January 1, 2005. The additional depreciation deduction is allowed for both regular tax and alternative minimum tax purposes for the taxable year in which the property is placed in service.[1] The basis of the property and the depreciation allowances in the year of purchase and later years is appropriately adjusted to reflect the additional first-year depreciation deduction. A taxpayer is allowed to elect out of the additional first-year depreciation for any class of property for any taxable year.

Property qualifies for the additional first-year depreciation deduction if the property is (1) property to which MACRS applies with a recovery period of 20 years or less other than leasehold improvements, (2) water utility property as defined in section 168(e)(5), or (3) computer software other than computer software covered by section 197. In order to be qualified property, the original use[2] of the property must commence with the taxpayer on or after September 11, 2001.[3] A special rule precludes the additional first-year depreciation deduction for property that is required to be depreciated under the alternative depreciation system of MACRS.

In addition, property qualifies only if acquired by the taxpayer (1) after September 10, 2001 and before September 11, 2004, and no binding written contract for the acquisition is in effect before September 11, 2001 or (2) pursuant to a binding written contract which was entered into after September 10, 2001, and before September 11, 2004. Finally, property that is manufactured, constructed, or produced by the taxpayer for use by the taxpayer qualifies if the taxpayer begins the manufacture, construction, or production of the property after September 10, 2001, and before September 11, 2004 (and all other requirements are met). Property that is manufactured, constructed, or produced for the taxpayer by another person under a contract that is entered into prior to the manufacture, construction, or production of the property is considered to be manufactured, constructed, or produced by the taxpayer.

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[1] The additional depreciation deduction is subject to the general rules regarding whether an item is deductible under section 162 or subject to capitalization under section 263 or section 263A.

[2] The term "original use" means the first use to which the property is put, whether or not such use corresponds to the use of such property by the taxpayer. Except as otherwise provided in Treasury Regulations, repaired or reconstructed property is not qualified property.

[3] A special rule applies in the case of certain leased property. In the case of any property that is originally placed in service by a person and that is sold to the taxpayer and leased back to such person by the taxpayer within three months after the date that the property was placed in service, the property is treated as originally placed in service by the taxpayer not earlier than the date that the property is used under the leaseback.

The limitation on the amount of depreciation deductions allowed with respect to certain passenger automobiles (sec. 280F of the Code) is increased in the first year by $4,600 for automobiles that qualify (and do not elect out of the increased first year deduction).

The following examples illustrate the operation of the provision.

Example 1.—Assume that on March 1, 2002, a calendar year taxpayer acquires and places in service qualified property that costs $1 million. Under the provision, the taxpayer is allowed an additional first-year depreciation deduction of $300,000. The remaining $700,000 of adjusted basis is to be recovered in 2002 and subsequent years pursuant to the depreciation rules of present law.

Example 2.—Assume that on March 1, 2002, a calendar year taxpayer acquires and places in service qualified property that costs $50,000. In addition, assume that the property qualifies for the expensing election under section 179. Under the provision, the taxpayer is first allowed a $35,000 deduction under section 179.[4] The taxpayer then is allowed an additional first-year depreciation deduction of $4,500 based on $15,000 ($50,000 original cost less the section 179 deduction of $35,000) of adjusted basis. Finally, the remaining adjusted basis of $11,500 ($15,000 adjusted basis less $4,500 additional first-year depreciation) is to be recovered in 2002 and subsequent years pursuant to the depreciation rules of present law.

EFFECTIVE DATE

The provision applies to property placed in service after September 10, 2001.

B. Temporary Increase in Section 179 Expensing (Sec. 102 of the Bill and Sec. 179 of the Code)

PRESENT LAW

Present law provides that, in lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $24,000 (for taxable years beginning in 2001 or 2002) of the cost of qualifying property placed in service for the taxable year (sec. 179). This amount is increased to $25,000 of the cost of qualified property placed in service for taxable years beginning in 2003 and thereafter. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $24,000 ($25,000 for taxable years beginning in 2003 and thereafter) amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $200,000. In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income for a taxable year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to similar limitations). No general business credit under section 38 is

[4] A subsequent provision in the bill temporarily increases the amount deductible under section 179 to $35,000.

allowed with respect to any amount for which a deduction is allowed under section 179.

REASONS FOR CHANGE

The Committee believes that increasing the number of small businesses eligible for immediate expensing and increasing the amount allowed to be expensed will provide an incentive for eligible businesses to increase their investment in capital assets, thus promoting economic growth for small businesses.

EXPLANATION OF PROVISION

The provision provides that the maximum dollar amount that may be deducted under section 179 is increased to $35,000 for property placed in service in taxable years beginning after December 31, 2001, and before January 1, 2004.[5] The provision increases the present law $200,000 limit to $325,000. Thus, under the provision the $35,000 amount is reduced by the amount by which the cost of qualifying property placed in service exceeds $325,000. As under present law, no general business credit under section 38 is allowed with respect to any amount for which a deduction is allowed under section 179. For taxable years beginning after December 31, 2003, present law applies (i.e., up to a $25,000 deduction that is reduced by the amount of qualifying property placed in service by the taxpayer that exceeds $200,000).

EFFECTIVE DATE

The provision is effective for taxable years beginning after December 31, 2001.

C. Repeal Corporate Alternative Minimum Tax (Sec. 103 of the Bill and Sec. 55 of the Code)

PRESENT LAW

In general

Present law imposes an alternative minimum tax ("AMT") on a corporation to the extent the corporation's tentative minimum tax exceeds its regular tax. This tentative minimum tax is computed at the rate of 20 percent on the alternative minimum taxable income ("AMTI") in excess of a $40,000 phased-out exemption amount. The exemption amount is phased out by an amount equal to 25 percent of the amount that the corporation's AMTI exceeds $150,000.

AMTI is the taxpayer's taxable income increased by certain preference items and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items.

A corporation with average gross receipts of less than $7.5 million for the prior three taxable years is exempt from the corporate minimum tax. The $7.5 million threshold is reduced to $5 million for the corporation's first 3-taxable year period.

[5] As a result of the increased deduction, the maximum dollar amount that may be deducted by an enterprise zone business or a renewal community business is increased to $70,000 for taxable years beginning after December 31, 2001, and before January 1, 2004. See sec. 1397A and sec. 1400J.

Preference items in computing AMTI

The corporate minimum tax preference items are:

(1) The excess of the deduction for percentage depletion over the adjusted basis of the property at the end of the taxable year. This preference does not apply to percentage depletion allowed with respect to oil and gas properties.

(2) The amount by which excess intangible drilling costs arising in the taxable year exceed 65 percent of the net income from oil, gas, and geothermal properties. This preference does not apply to an independent producer to the extent the preference would not reduce the producer's AMTI by more than 40 percent.

(3) Tax-exempt interest income on private activity bonds (other than qualified 501(c)(3) bonds) issued after August 7, 1986.

(4) Accelerated depreciation or amortization on certain property placed in service before January 1, 1987.

Adjustments in computing AMTI

The adjustments that corporations must make in computing AMTI are:

(1) Depreciation on property placed in service after 1986 and before January 1, 1999, must be computed by using the generally longer class lives prescribed by the alternative depreciation system of section 168(g) and either (a) the straight-line method in the case of property subject to the straight-line method under the regular tax or (b) the 150-percent declining balance method in the case of other property. Depreciation on property placed in service after December 31, 1998, is computed by using the regular tax recovery periods and the AMT methods described in the previous sentence.

(2) Mining exploration and development costs must be capitalized and amortized over a 10-year period.

(3) Taxable income from a long-term contract (other than a home construction contract) must be computed using the percentage of completion method of accounting.

(4) The amortization deduction allowed for pollution control facilities placed in service before January 1, 1999 (generally determined using 60-month amortization for a portion of the cost of the facility under the regular tax), must be calculated under the alternative depreciation system (generally, using longer class lives and the straight-line method). The amortization deduction allowed for pollution control facilities placed in service after December 31, 1998, is calculated using the regular tax recovery periods and the straight-line method.

(5) The special rules applicable to Merchant Marine construction funds are not applicable.

(6) The special deduction allowable under section 833(b) for Blue Cross and Blue Shield organizations is not allowed.

(7) The adjusted current earnings adjustment applies, as described below.

Adjusted current earning ("ACE") adjustment

The adjusted current earnings adjustment is the amount equal to 75 percent of the amount by which the adjusted current earnings of a corporation exceeds its AMTI (determined without the ACE adjustment and the alternative tax net operating loss deduction). In determining ACE the following rules apply:

(1) For property placed in service before 1994, depreciation generally is determined using the straight-line method and the class life determined under the alternative depreciation system.

(2) Any amount that is excluded from gross income under the regular tax but is included for purposes of determining earnings and profits is included in determining ACE.

(3) The inside build-up of a life insurance contract is included in ACE (and the related premiums are deductible).

(4) Intangible drilling costs of integrated oil companies must be capitalized and amortized over a 60-month period.

(5) The regular tax rules of section 173 (allowing circulation expenses to be amortized) and section 248 (allowing organizational expenses to be amortized) do not apply.

(6) Inventory must be calculated using the FIFO, rather than LIFO, method.

(7) The installment sales method generally may not be used.

(8) No loss may be recognized on the exchange of any pool of debt obligations for another pool of debt obligations having substantially the same effective interest rates and maturities.

(9) Depletion (other than for oil and gas) must be calculated using the cost, rather than the percentage, method.

(10) In certain cases, the assets of a corporation that has undergone an ownership change must be stepped-down to their fair market values.

Other rules

The combination of the taxpayer's net operating loss carryover and foreign tax credits cannot reduce the taxpayer's AMT liability by more than 90 percent of the amount determined without these items.

The various nonrefundable business credits allowed under the regular tax generally are not allowed against the AMT.

If a corporation is subject to AMT in any year, the amount of AMT is allowed as a credit ("AMT credit") in any subsequent taxable year to the extent the taxpayer's regular tax liability exceeds its tentative minimum tax in the subsequent year.

REASONS FOR CHANGE

The Committee believes that the corporate AMT inhibits capital formation and business enterprise, and is administratively complex. During an economic slowdown, corporations are more likely to be liable for the AMT because their income is low relative to their investment in plant and equipment. Therefore, the bill repeals the corporate AMT.

EXPLANATION OF PROVISION

The provision repeals the corporate AMT.

The provision makes the AMT credit for corporations refundable.[6] Thus, a corporation will be able to obtain a refund of its en-

[6] Because the AMT credit will be refunded in the corporation's first taxable year beginning after December 31, 2000, the computation of the AMT, and the computation of the tentative minimum tax for purposes of the credits allowed by sections 29 and 30, will not take into account any carrybacks from taxable years beginning after that date.

In computing the tentative minimum tax for purposes of computing the AMT credit for a taxable year beginning before 2001, carrybacks from taxable years beginning after 2000 likewise will not be taken into account. To the extent the AMT credit is reduced in a prior taxable year

tire AMT credit for the first taxable year beginning after December 31, 2000 (to the extent the credit is in excess of tax liability).

EFFECTIVE DATE

The provision applies to taxable years beginning after December 31, 2000.

D. Temporary Extension of the Net Operating Loss Carryback Period (Sec. 104 of the Bill and Secs. 172 and 56 of the Code)

PRESENT LAW

A net operating loss ("NOL") is, generally, the amount by which a taxpayer's allowable deductions exceed the taxpayer's gross income. An NOL that is carried back may be deducted from gross income in the carryback year, thereby resulting in a refund of Federal income tax for the carryback year. Similarly, an NOL that is carried forward may be deducted from gross income in a carryforward year, thus reducing the Federal income tax liability for the carryforward year.

In general, an NOL may be carried back two years and carried forward 20 years to offset taxable income in such years. Different rules apply with respect to NOLs arising in certain circumstances. For example, a three-year carryback applies with respect to NOLs (1) arising from casualty or theft losses of individuals, or (2) attributable to Presidentially declared disasters for taxpayers engaged in a farming business or a small business. A five-year carryback period applies to NOLs from a farming loss (regardless of whether the loss was incurred in a Presidentially declared disaster area). Special rules also apply to real estate investment trusts (no carryback), specified liability losses (10-year carryback), and excess interest losses (no carryback).

The alternative minimum tax rules provide that a taxpayer's NOL deduction cannot reduce the taxpayer's alternative minimum taxable income ("AMTI") by more than 90 percent of the AMTI.

REASONS FOR CHANGE

The NOL carryback and carryforward rules allow taxpayers to smooth out swings in business income (and Federal income taxes thereon) that result from business cycle fluctuations and unexpected financial losses. The current uncertain economic conditions have resulted in many taxpayers incurring unexpected financial losses. A temporary extension of the NOL carryback period will provide taxpayers in all sectors of the economy who experience such losses the ability to increase their cash flow through the refund of income taxes paid in prior years. The provision will free up funds that can be used for capital investment or other expenses that will provide stimulus to the economy.

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as a result of this rule, the AMT credit will be allowed or refunded in a later taxable year. Under the rules relating to the computation of interest resulting from carrybacks, any resulting decreases and increases in the AMT credit in differing taxable years resulting from a post-2000 carryback should offset each other.

In computing the general business credit for a taxable year beginning before 2001, the tentative minimum tax will be computing using the same amount of carryback from taxable years beginning after 2000 as used for purposes of computing the regular tax.

EXPLANATION OF PROVISION

The provision temporarily extends the general NOL carryback period to five years (from two years) for NOLs arising in taxable years ending on or after September 11, 2001, and ending before September 11, 2004. In addition, the five-year carryback period applies to NOLs from these years that qualify under present law for a three-year carryback period (i.e., NOLs arising from casualty or theft losses of individuals or attributable to certain Presidentially declared disaster areas).

The provision also allows an NOL deduction attributable to these taxable years to offset 100 percent of a taxpayer's AMTI in a carryback year.[7]

A taxpayer can elect to forgo the five-year carryback period. The election to forgo the five-year carryback period is made in the manner prescribed by the Secretary of the Treasury and must be made by the due date of the return (including extensions) for the year of the loss. The election is irrevocable. If a taxpayer elects to forgo the five-year carryback period, then the losses are subject to the rules that otherwise would apply under section 172 absent the provision.

EFFECTIVE DATE

The provision is effective for NOLs arising in taxable years ending on or after September 11, 2001, and before September 11, 2004.

E. Treatment of Leasehold Improvements (Sec. 105 of the Bill and Sec. 168 of the Code)

PRESENT LAW

Depreciation of leasehold improvements

Depreciation allowances for property used in a trade or business generally are determined under the modified Accelerated Cost Recovery System ("MACRS") of section 168. Depreciation allowances for improvements made on leased property are determined under MACRS, even if the MACRS recovery period assigned to the property is longer than the term of the lease (sec. 168(i)(8)).[8] This rule applies regardless whether the lessor or lessee places the leasehold improvements in service.[9] If a leasehold improvement constitutes an addition or improvement to nonresidential real property already placed in service, the improvement is depreciated using the straight-line method over a 39-year recovery period, beginning in the month the addition or improvement was placed in service (secs. 168(b)(3), (c)(1), (d)(2), and (i)(6)).[10]

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[7] Section 172(b)(2) should be appropriately applied in computing AMTI to take proper account of the order that the NOL carryovers and carrybacks are used as a result of this provision. See section 56(d)(1)(B)(ii).

[8] The Tax Reform Act of 1986 modified the Accelerated Cost Recovery System ("ACRS") to institute MACRS. Prior to the adoption of ACRS by the Economic Recovery Act of 1981, taxpayers were allowed to depreciate the various components of a building as separate assets with separate useful lives. The use of component depreciation was repealed upon the adoption of ACRS. The Tax Reform Act of 1986 also denied the use of component depreciation under MARCS.

[9] Former Code sections 168(f)(6) and 178 provided that in certain circumstances, a lessee could recover the cost of leasehold improvements made over the remaining term of the lease. These provisions were repealed by the Tax Reform Act of 1986.

[10] If the improvement is characterized as tangible personal property, ACRS or MARCS depreciation is calculated using the shorter recovery periods and accelerated methods applicable to such property. The determination of whether certain improvements are characterized as tangible personal property or as nonresidential real property often depends on whether or not the

Treatment of dispositions of leasehold improvements

A lessor of leased property that disposes of a leasehold improvement which was made by the lessor for the lessee of the property may take the adjusted basis of the improvement into account for purposes of determining gain or loss if the improvement is irrevocably disposed of or abandoned by the lessor at the termination of the lease.[11] This rule conforms the treatment of lessors and lessees with respect to leasehold improvements disposed of at the end of a term of lease. For purposes of applying this rule, it is expected that a lessor must be able to separately account for the adjusted basis of the leasehold improvement that is irrevocably disposed of or abandoned. This rule does not apply to the extent section 280B applies to the demolition of a structure, a portion of which may include leasehold improvements.[12]

REASONS FOR CHANGE

The Committee believes that costs of certain leasehold improvements should not be recovered beyond the term of the lease to the extent that the costs do not provide a future benefit beyond that term. Although lease terms differ, the Committee believes that lease terms for commercial real estate typically are shorter than the present-law 39-year recovery period. In the interests of simplicity and administrability, a uniform period for recovery of leasehold improvements is desirable. The Committee bill therefore shortens the recovery period for leasehold improvements to 15 years.

EXPLANATION OF PROVISION

The provision provides that 15-year property for purposes of the depreciation rules of section 168 includes qualified leasehold improvement property. The straight line method is required to be used with respect to qualified leasehold improvement property.

Qualified leasehold improvement property is any improvement to an interior portion of a building that is nonresidential real property, provided certain requirements are met. The improvement must be made under or pursuant to a lease either by the lessee (or sublessee) of that portion of the building, or by the lessor of that portion of the building. That portion of the building is to be occupied exclusively by the lessee (or any sublessee). The improvement must be placed in service more than three years after the date the building was first placed in service.

Qualified leasehold improvement property does not include any improvement for which the expenditure is attributable to the enlargement of the building, any elevator or escalator, any structural component benefiting a common area, or the internal structural framework of the building.

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improvements constitute a "structural component" of a building (as defined by Treas. Reg. sec. 1.48–1(e)(1)). See, for example, *Metro National Corp.,* 52 TCM 1440 (1987); *King Radio Corp.,* 486 F.2d 1091 (10th Cir., 1973); *Mallinckrodt, Inc.,* 778 F.2d 402 (8th Cir., 1985) (with respect various leasehold improvements).

[11] The conference report describing this provision mistakenly states that the provision applies to improvements that are irrevocably disposed of or abandoned by the lessee (rather than the lessor) at the termination of the lease.

[12] Undere present law, section 280B denies a deduction for any loss sustained on the demolition of any structure.

A 15-year period is specified as the class life of qualified leasehold improvement property for purposes of the alternative depreciation system. Therefore, the general rule that the class life for nonresidential real and residential rental property is 40 years does not apply to qualified leasehold improvement property.

For purposes of the provision, a commitment to enter into a lease is treated as a lease, and the parties to the commitment are treated as lessor and lessee. A lease between related persons is not considered a lease for this purpose.

Under the provision, an improvement made by the person who was the lessor of the improvement when it was placed in service generally is treated as qualified leasehold improvement property only so long as the improvement is held by that person. Exceptions are provided under this rule in the case of certain changes in the form of business. Under these exceptions, property does not cease to be qualified leasehold improvement property under the provision by reason of (1) death, (2) a transaction to which section 381 (relating to carryovers in certain corporate acquisitions) applies, or (3) a mere change in the form of conducting the trade or business so long as the property is retained in the business as qualified leasehold improvement property and the taxpayer retains a substantial interest in the business.

Qualified leasehold improvement property is not eligible for the 30 percent expensing provided under a separate provision of the bill.

EFFECTIVE DATE

The provision is effective for qualified leasehold improvement property placed in service on or after September 11, 2001.

TITLE II: INDIVIDUAL PROVISIONS

A. Accelerate the 25-Percent Rate Bracket to 2002 (Sec. 201(a) of the Bill and Sec. 1 of the Code)

PRESENT LAW

The Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") reduced the prior-law 28-percent individual regular income tax rate to 25 percent. This rate reduction is phased-in over six years. The rate is 27 percent for taxable years beginning in calendar years 2001–2003,[13] 26 percent for taxable years beginning in calendar years 2004–2005, and 25 percent for taxable years beginning in calendar years 2006 and thereafter.

REASONS FOR CHANGE

The Committee believes that this stimulus package should contain provisions targeted at both businesses and individuals. Further, the Committee believes that the acceleration of the rate reduction of the 28-percent individual regular income tax rate provided in EGTRRA is an appropriate element of this fiscal stimulus tax package. Accelerating the decrease in the 28-percent rate bracket will allow taxpayers to keep more of their own money

[13] A blended rate of 27.5 percent applies in 2001 because of the July 1, 2001 effective date of EGTRRA.

starting in 2002 and provide additional funds for needed consumer purchases. In addition, accelerating the rate reduction will increase the after-tax rate of return for many small businesses. Thus, the Committee believes that acceleration of the rate reduction will stimulate the economy by increasing consumer confidence and spending and spurring economic activity.

EXPLANATION OF PROVISIONS

The bill provides that the 25-percent rate is effective for taxable years beginning in calendar years 2002 and thereafter.

EFFECTIVE DATE

The provision is effective for taxable years beginning after December 31, 2001.

B. Alternative Minimum Tax Exemption for Individuals (Sec. 201(b) of the Bill and Sec. 55 of the Code)

PRESENT LAW

The alternative minimum tax is the amount by which the tentative minimum tax exceeds the regular income tax. An individual's tentative minimum tax is an amount equal to (1) 26 percent of the first $175,000 ($87,500 in the case of a married individual filing a separate return) of alternative minimum taxable income ("AMTI") in excess of a phased-out exemption amount and (2) 28 percent of the remaining AMTI. The maximum tax rates on net capital gain used in computing the tentative minimum tax are the same as under the regular tax. AMTI is the individual's taxable income adjusted to take account of specified preferences and adjustments. The exemption amounts are: (1) $45,000 ($49,000 in taxable years beginning before 2005) in the case of married individuals filing a joint return and surviving spouses; (2) $33,750 ($35,750 in taxable years beginning before 2005) in the case of other unmarried individuals; (3) $22,500 ($24,500 in taxable years beginning before 2005) in the case of married individuals filing a separate return; and (4) $22,500 in the case of an estate or trust. The exemption amounts are phased out by an amount equal to 25 percent of the amount by which the individual's AMTI exceeds (1) $150,000 in the case of married individuals filing a joint return and surviving spouses, (2) $112,500 in the case of other unmarried individuals, and (3) $75,000 in the case of married individuals filing separate returns or an estate or a trust. These amounts are not indexed for inflation.

REASONS FOR CHANGE

The Committee believes that an adjustment to the AMT exemption amount is necessary to allow the bill's acceleration in the 25-percent rate bracket to have full effect. Without an adjustment, the AMT would reduce the benefit of the rate reduction for many individuals, thereby reducing the stimulative effect of the rate reduction.

EXPLANATION OF PROVISION

The provision increases the AMT exemption amount of individuals for taxable years beginning in 2002, 2003, and 2004.

For 2002 and 2003, the $49,000 exemption amount is increased by $3,200; the $35,750 exemption amount is increased by $1,600; and the $24,500 exemption amount is increased by $1,600.

For 2004, the $49,000 exemption amount is increased by $1,700; the $35,750 exemption amount is increased by $850; and the $24,500 exemption amount is increased by $850.

EFFECTIVE DATE

The provision is effective for taxable years beginning after December 31, 2001 and before January 1, 2005.

C. Simplify Individual Capital Gains Rates (Sec. 202 of the Bill and Sec. 1(h) of the Code)

PRESENT LAW

In general, gain or loss reflected in the value of an asset is not recognized for income tax purposes until a taxpayer disposes of the asset. On the sale or exchange of a capital asset, any gain generally is included in income. Any net capital gain of an individual is taxed at maximum rates lower than the rates applicable to ordinary income. Net capital gain is the excess of the net long-term capital gain for the taxable year over the net short-term capital loss for the year. Gain or loss is treated as long-term if the asset is held for more than one year.

Capital losses generally are deductible in full against capital gains. In addition, individual taxpayers may deduct capital losses against up to $3,000 of ordinary income in each year. Any remaining unused capital losses may be carried forward indefinitely to another taxable year.

A capital asset generally means any property except (1) inventory, stock in trade, or property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business, (2) depreciable or real property used in the taxpayer's trade or business, (3) specified literary or artistic property, (4) business accounts or notes receivable, (5) certain U.S. publications, (6) certain commodity derivative financial instruments, (7) hedging transactions, and (8) business supplies. In addition, the net gain from the disposition of certain property used in the taxpayer's trade or business is treated as long-term capital gain. Gain from the disposition of depreciable personal property is not treated as capital gain to the extent of all previous depreciation allowances. Gain from the disposition of depreciable real property is generally not treated as capital gain to the extent of the depreciation allowances in excess of the allowances that would have been available under the straight-line method of depreciation.

The maximum rate of tax on the adjusted net capital gain of an individual is 20 percent. In addition, any adjusted net capital gain which otherwise would be taxed at a 15-percent rate is taxed at a 10-percent rate. These rates apply for purposes of both the regular tax and the alternative minimum tax.

The "adjusted net capital gain" of an individual is the net capital gain reduced (but not below zero) by the sum of the 28-percent rate gain and the unrecaptured section 1250 gain. The net capital gain is reduced by the amount of gain that the individual treats as investment income for purposes of determining the investment interest limitation under section 163(d).

The term "28-percent rate gain" means the amount of net gain attributable to long-term capital gains and losses from the sale or exchange of collectibles (as defined in section 408(m) without regard to paragraph (3) thereof), an amount of gain equal to the amount of gain excluded from gross income under section 1202 (relating to certain small business stock),[14] the net short-term capital loss for the taxable year, and any long-term capital loss carryover to the taxable year.

"Unrecaptured section 1250 gain" means any long-term capital gain from the sale or exchange of section 1250 property (i.e., depreciable real estate) held more than one year to the extent of the gain that would have been treated as ordinary income if section 1250 applied to all depreciation, reduced by the net loss (if any) attributable to the items taken into account in computing 28-percent rate gain. The amount of unrecaptured section 1250 gain (before the reduction for the net loss) attributable to the disposition of property to which section 1231 applies shall not exceed the net section 1231 gain for the year.

The unrecaptured section 1250 gain is taxed at a maximum rate of 25 percent, and the 28-percent rate gain is taxed at a maximum rate of 28 percent. Any amount of unrecaptured section 1250 gain or 28-percent rate gain otherwise taxed at a 15-percent rate is taxed at the 15-percent rate.

Any gain from the sale or exchange of property held more than five years which would otherwise be taxed at the 10-percent rate is taxed at an 8-percent rate. Any gain from the sale or exchange of property held more than five years and the holding period for which begins after December 31, 2000, which would otherwise be taxed at a 20-percent rate is taxed at an 18-percent rate.

A taxpayer holding a capital asset or property used in the trade or business on January 1, 2001, may elect to treat the asset as having been sold on that date for an amount equal to its fair market value, and having been reacquired for an amount equal to such value.

REASONS FOR CHANGE

The bill simplifies the capital gain rates by eliminating the 5-year holding period so that the 8- and 18-percent rates are effective for assets held more than one year, and the 10- and 20-percent rates will no longer apply.

EXPLANATION OF PROVISION

The provision reduces the 10- and 20-percent rates on the adjusted net capital gain to 8 and 18 percent, respectively. These lower rates apply to both the regular tax and the alternative minimum tax.

[14] This results in a maximum effective regular tax rate on qualified gain from small business stock of 14 percent.

The provision repeals the special rules for certain gain from property held more than 5 years, and repeals the election to recognize gain on property held on January 1, 2001. The lower rates apply to assets held more than one year.

EFFECTIVE DATE

The provision applies to taxable years of individual taxpayers ending on or after October 12, 2001.

For taxable years of individual taxpayers that include October 12, 2001, the lower rates apply to amounts properly taken into account for the portion of the year on or after that date. This generally has the effect of applying the lower rates to capital assets sold or exchanged (and installment payments received) on or after October 12, 2001. In the case of gain taken into account by a passthrough entity, the date taken into account by the entity is the appropriate date for applying this rule (without regard to the taxable year of the entity).

D. Increase Deduction of Capital Losses of Individuals Against Ordinary Income (Sec. 203 of the Bill and Sec. 1211 of the Code)

PRESENT LAW

Capital losses of individuals are deductible in full against capital gains. In addition, individual taxpayers may deduct capital losses against up to $3,000 ($1,500 in the case of married individuals filing a separate return) of ordinary income in each taxable year. Any remaining unused capital losses may be carried forward indefinitely to future taxable years.

REASONS FOR CHANGE

The Committee believes that the limitation on the deductibility of capital losses should be raised.

EXPLANATION OF PROVISION

The amount of capital losses of individuals that may offset ordinary income is increased from $3,000 to $4,000 in taxable years beginning in 2001 and to $5,000 in taxable years beginning in 2002. For married individuals filing a separate return, the increases are from $1,500 to $2,000 and $2,500 respectively.

EFFECTIVE DATE

The provision applies to taxable years beginning in 2001 and 2002.

E. Expand Exception From Early Withdrawal Tax for Health Insurance Expenses of Unemployed Individuals (Sec. 204 of the Bill and Sec. 72(t) of the Code)

PRESENT LAW

A distribution from an individual retirement account ("IRA") or an employer-sponsored retirement plan generally is includible in gross income in the year it is paid under the rules relating to taxation of annuities, unless the amount distributed represents the in-

dividual's investment in the contract (i.e., basis). Special rules apply in the case of Roth IRAs, distributions that are rolled over into another tax-favored retirement plan, distributions of employer securities, and certain other situations.

Taxable distributions made from an IRA or from certain employer-sponsored retirement plans before age 59½, death, or disability generally are subject to an additional 10-percent income tax. Besides IRAs, the early withdrawal tax applies to distributions from a qualified retirement plan (including a section 401(k) plan), a qualified annuity plan, or a tax-deferred annuity plan ("section 403(b) plan"). However, exceptions apply to the early withdrawal tax, depending in part on the specific type of arrangement from which the distribution is made and the purpose for which the distribution is used.

The 10-percent early withdrawal tax does not apply to IRA distributions to an unemployed individual after separation from employment to the extent the distributions do not exceed the amount paid during the year for health insurance for the individual and the individual's spouse and dependents. This exception applies if the individual (including a self-employed individual) has received unemployment compensation under Federal or State law for at least 12 consecutive weeks and if the distribution is made in the year such unemployment compensation is received or the following year. If a self-employed individual is not eligible for unemployment compensation under applicable law, then, to the extent provided in regulations, a self-employed individual is treated as having received unemployment compensation for at least 12 weeks if the individual would have received unemployment compensation but for the fact that the individual was self-employed.

The exception to the early withdrawal tax ceases to apply if the individual has been reemployed for at least 60 days.

REASONS FOR CHANGE

The Committee understands that individuals who lose their jobs as a result of the current economic downturn may face unexpected health insurance costs. The Committee believes that it is appropriate to provide a temporary exception to the early withdrawal tax for individuals who withdraw retirement funds in order to pay for health insurance.

EXPLANATION OF PROVISION

The provision temporarily expands the present-law exception to the early withdrawal tax for IRA distributions used for health insurance for unemployed individuals. Under the provision, the exception applies to distributions made after separation from employment to individuals who receive unemployment compensation for four consecutive weeks during the period from September 11, 2001 to December 31, 2002. As under present law, the exception applies to the extent distributions do not exceed the amount paid during the year for health insurance for the individual and the individual's spouse and dependents. As under present law, the exception can apply to distributions made in the year following the year in which the unemployment compensation is received, but does not apply to distributions made after the individual has been reemployed for at least 60 days.

Under the provision, the exception applies also to distributions from a qualified retirement plan (including a section 401(k) plan), a qualified annuity plan, or a section 403(b) plan, provided the requirements for the exception are otherwise met.

EFFECTIVE DATE

The provision is effective for distributions made after the date of enactment.

TITLE III: EXTENSIONS OF EXPIRING PROVISIONS

A. Two-Year Extension of Provisions Expiring in 2001

1. Extend Alternative Minimum Tax Relief for Individuals (sec. 301 of the bill and sec. 26 of the Code)

PRESENT LAW

Present law provides for certain nonrefundable personal tax credits (i.e., the dependent care credit, the credit for the elderly and disabled, the adoption credit, the child tax credit[15], the credit for interest on certain home mortgages, the HOPE Scholarship and Lifetime Learning credits, the IRA credit, and the D.C. homebuyer's credit). For taxable years beginning after 2001, these credits (other than the adoption credit, child credit and IRA credit) are allowed only to the extent that the individual's regular income tax liability exceeds the individual's tentative minimum tax, determined without regard to the minimum tax foreign tax credit. The adoption credit, child credit, and IRA credit are allowed to the full extent of the individual's regular tax and alternative minimum tax.

For taxable years beginning in 2001, all the nonrefundable personal credits are allowed to the extent of the full amount of the individual's regular tax and alternative minimum tax.

The alternative minimum tax is the amount by which the tentative minimum tax exceeds the regular income tax. An individual's tentative minimum tax is an amount equal to (1) 26 percent of the first $175,000 ($87,500 in the case of a married individual filing a separate return) of alternative minimum taxable income ("AMTI") in excess of a phased-out exemption amount and (2) 28 percent of the remaining AMTI. The maximum tax rates on net capital gain used in computing the tentative minimum tax are the same as under the regular tax. AMTI is the individual's taxable income adjusted to take account of specified preferences and adjustments. The exemption amounts are: (1) $45,000 ($49,000 in taxable years beginning before 2005) in the case of married individuals filing a joint return and surviving spouses; (2) $33,750 ($35,750 in taxable years beginning before 2005) in the case of other unmarried individuals; (3) $22,500 ($24,500 in taxable years beginning before 2005) in the case of married individuals filing a separate return; and (4) $22,500 in the case of an estate or trust.[16] The exemption amounts are phased out by an amount equal to 25 percent of the amount by which the individual's AMTI exceeds (1) $150,000 in the case of married individuals filing a joint return and surviving spouses, (2) $112,500 in the case of other unmarried individuals,

[15] A portion of the child credit may be refundable.
[16] Section 202(b) of the bill increases certain of the exemption amounts.

and (3) $75,000 in the case of married individuals filing separate returns or an estate or a trust. These amounts are not indexed for inflation.

REASONS FOR CHANGE

The Committee believes that the nonrefundable personal credits should be useable without limitation by reason of the alternative minimum tax. This will result in significant simplification.

EXPLANATION OF PROVISION

The provision allows an individual to offset the entire regular tax liability and alternative minimum tax liability by the personal nonrefundable credits in 2002 and 2003.

EFFECTIVE DATE

The provision is effective for taxable years beginning in 2002 and 2003.

2. Extend Credit for Purchase of Electric Vehicles (sec. 302 of the bill and secs. 30 and 280F of the Code)

A 10-percent tax credit is provided for the cost of a qualified electric vehicle, up to a maximum credit of $4,000 (sec. 30). A qualified electric vehicle is a motor vehicle that is powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electrical current, the original use of which commences with the taxpayer, and that is acquired for the use by the taxpayer and not for resale. The full amount of the credit is available for purchases prior to 2002. The credit phases down in the years 2002 through 2004, and is unavailable for purchases after December 31, 2004.[17]

REASONS FOR CHANGE

The Committee believes that continued economic incentive is warranted to increase the presence of electric vehicles on the nation's roadways.

EXPLANATION OF PROVISION

The bill defers the phase down of the credit by two years. Taxpayers may claim the full amount of the credit for qualified purchases made in 2002 and 2003. Under the bill, the phase down of the credit value commences in 2004 and the credit is unavailable for purchases after December 31, 2006. A conforming modification is made to section 280F.

EFFECTIVE DATE

The provision is effective on the date of enactment.

[17] The amount the taxpayer may claim as a depreciation deduction for any passenger automobile is limited (sec. 280F). In the case of a passenger vehicle designed to be propelled primarily by electricity and built by an original equipment manufactgurer, the otherwise applicable limitation amounts are tripled. These exceptions from sec. 280F apply to vehicles placed in service prior to January 1, 2005.

3. Extend Section 45 Credit for Production of Electricity from Wind, Closed Loop Biomass, and Poultry Litter (sec. 303 of the bill and sec. 45 of the Code)

PRESENT LAW

An income tax credit is allowed for the production of electricity from either qualified wind energy, qualified "closed-loop" biomass, or qualified poultry waste facilities (sec. 45).

The credit applies to electricity produced by a wind energy facility placed in service after December 31, 1993, and before January 1, 2002, to electricity produced by a closed-loop biomass facility placed in service after December 31, 1992, and before January 1, 2002, and to a poultry waste facility placed in service after December 31, 1999, and before January 1, 2002. The credit is allowable for production during the 10-year period after a facility is originally placed in service. In order to claim the credit, a taxpayer must own the facility and sell the electricity produced by the facility to an unrelated party. In the case of a poultry waste facility, the taxpayer may claim the credit as a lessee/operator of a facility owned by a governmental unit.

Closed-loop biomass is plant matter, where the plants are grown for the sole purpose of being used to generate electricity. It does not include waste materials (including, but not limited to, scrap wood, manure, and municipal or agricultural waste). The credit also is not available to taxpayers who use standing timber to produce electricity. Poultry waste means poultry manure and litter, including wood shavings, straw, rice hulls, and other bedding material for the disposition of manure.

The credit for electricity produced from wind, closed-loop biomass, or poultry waste is a component of the general business credit (sec. 38(b)(8)). The credit, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000, or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39). To coordinate the carryback with the period of application for this credit, the credit for electricity produced from closed-loop biomass facilities may not be carried back to a tax year ending before 1993 and the credit for electricity produced from wind energy may not be carried back to a tax year ending before 1994 (sec. 39).

REASONS FOR CHANGE

The Committee believes that continued economic incentive is warranted to increase the presence of these more environmentally friendly generation sources in the nation's electricity grid.

EXPLANATION OF PROVISION

The bill extends the placed in service date for qualified facilities by two years to include those facilities placed in service prior to January 1, 2004.

EFFECTIVE DATE

The provision is effective on the date of enactment.

4. Extend the Work Opportunity Tax Credit (sec. 304 of the bill and sec. 51 of the Code)

PRESENT LAW

In general

The work opportunity tax credit ("WOTC") is available on an elective basis for employers hiring individuals from one or more of eight targeted groups. The credit equals 40 percent (25 percent for employment of less than 400 hours) of qualified wages. Generally, qualified wages are wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer.

The maximum credit per employee is $2,400 (40 percent of the first $6,000 of qualified first-year wages). With respect to qualified summer youth employees, the maximum credit is $1,200 (40 percent of the first $3,000 of qualified first-year wages).

For purposes of the credit, wages are generally defined as under the Federal Unemployment Tax Act, without regard to the dollar cap.

Targeted groups eligible for the credit

The eight targeted groups are: (1) families eligible to receive benefits under the Temporary Assistance for Needy Families ("TANF") Program; (2) high-risk youth; (3) qualified ex-felons; (4) vocational rehabilitation referrals; (5) qualified summer youth employees; (6) qualified veterans; (7) families receiving food stamps; and (8) persons receiving certain Supplemental Security Income ("SSI") benefits.

The employer's deduction for wages is reduced by the amount of the credit.

Expiration date

The credit is effective for wages paid or incurred to a qualified individual who begins work for an employer before January 1, 2002.

REASONS FOR CHANGE

The Committee believes that a temporary extension of this credit will allow the Congress and the Treasury and Labor Departments to continue to monitor the effectiveness of the credit.

EXPLANATION OF PROVISION

The bill extends the work opportunity tax credit for two years (through December 31, 2003).

EFFECTIVE DATE

The provision is effective for wages paid or incurred to a qualified individual who begins work for an employer on or after January 1, 2002, and before January 1, 2004.

5. Extend the Welfare-To-Work Tax Credit (sec. 305 of the bill and sec. 51A of the Code)

PRESENT LAW

In general

The welfare-to-work tax credit is available on an elective basis for employers for the first $20,000 of eligible wages paid to qualified long-term family assistance recipients during the first two years of employment. The credit is 35 percent of the first $10,000 of eligible wages in the first year of employment and 50 percent of the first $10,000 of eligible wages in the second year of employment. The maximum credit is $8,500 per qualified employee.

Qualified long-term family assistance recipients are: (1) members of a family that has received family assistance for at least 18 consecutive months ending on the hiring date; (2) members of a family that has received family assistance for a total of at least 18 months (whether or not consecutive) after the date of enactment of this credit if they are hired within 2 years after the date that the 18–month total is reached; and (3) members of a family that is no longer eligible for family assistance because of either Federal or State time limits, if they are hired within two years after the Federal or State time limits made the family ineligible for family assistance. Family assistance means benefits under the Temporary Assistance to Needy Families ("TANF") program.

For purposes of the credit, wages are generally defined under the Federal Unemployment Tax Act, without regard to the dollar amount. In addition, wages include the following: (1) educational assistance excludable under a section 127 program; (2) the value of excludable health plan coverage but not more than the applicable premium defined under section 4980B(f)(4); and (3) dependent care assistance excludable under section 129.

The employer's deduction for wages is reduced by the amount of the credit.

Expiration date

The welfare to work credit is effective for wages paid or incurred to a qualified individual who begins work for an employer before January 1, 2002.

REASONS FOR CHANGE

The Committee believes that the welfare-to-work credit should be temporarily extended to provide the Congress and Treasury and Labor Departments a better opportunity to assess the operation and effectiveness of the credit in meeting its goals. These goals are: (1) to provide an incentive to hire long-term welfare recipients; (2) to promote the transition from welfare to work by increasing access to employment for these individuals; and (3) to encourage employers to provide these individuals with training, health coverage, dependent care and ultimately better job attachment.

EXPLANATION OF PROVISION

The bill extends the welfare to work credit for two years (through December 31, 2003).

EFFECTIVE DATE

The provision is effective for wages paid or incurred to a qualified individual who begins work for an employer on or after January 1, 2002, and before January 1, 2004.

6. Extend Deduction for Qualified Clean-Fuel Vehicle Property and Qualified Clean-Fuel Vehicle Refueling Property (sec. 306 of the bill and secs. 179A and 280F of the Code)

Certain costs of qualified clean-fuel vehicle property and clean-fuel vehicle refueling property may be expensed and deducted when such property is placed in service (sec. 179A).[18] Qualified clean-fuel vehicle property includes motor vehicles that use certain clean-burning fuels (natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, electricity and any other fuel at least 85 percent of which is methanol, ethanol, any other alcohol or ether). The maximum amount of the deduction is $50,000 for a truck or van with a gross vehicle weight over 26,000 pounds or a bus with seating capacities of at least 20 adults; $5,000 in the case of a truck or van with a gross vehicle weight between 10,000 and 26,000 pounds; and $2,000 in the case of any other motor vehicle. Qualified electric vehicles do not qualify for the clean-fuel vehicle deduction.

Clean-fuel vehicle refueling property comprises property for the storage or dispensing of a clean-burning fuel, if the storage or dispensing is the point at which the fuel is delivered into the fuel tank of a motor vehicle. Clean-fuel vehicle refueling property also includes property for the recharging of electric vehicles, but only if the property is located at a point where the electric vehicle is recharged. Up to $100,000 of such property at each location owned by the taxpayer may be expensed with respect to that location.

The deduction for clean-fuel vehicle property phases down in the years 2002 through 2004, and is unavailable for purchases after December 31, 2004. The deduction for clean-fuel vehicle refueling property is unavailable for property placed in service after December 31, 2004.

REASONS FOR CHANGE

The Committee believes that continued economic incentive is warranted to increase the presence of alternative fuel vehicles in the market.

EXPLANATION OF PROVISION

The bill defers the phase down of the deduction for clean-fuel vehicle property by two years. Taxpayers may claim the full amount of the deduction for qualified vehicles placed in service in 2002 and 2003. Under the bill, the phase down of the deduction for clean-fuel vehicles commences in 2004 and the deduction is unavailable for

[18] The amount the taxpayer may claim as a depreciation deduction for any passenger automobile is limited (sec. 280F). In the case of a qualified clean-burning fuel vehicle, the limitation of sec. 280F applies only to that portion of the vehicle's cost not represented by the installed qualified clean-burning fuel property. The taxpayer may claim an amount otherwise allowable as a depreciation deduction on the installed qualified clean-burning fuel property, without regard to the limitation. These exceptions from sec. 280F apply to vehicles placed in service prior to January 1, 2005.

purchases after December 31, 2006. A conforming modification is made to section 280F.

The provision extends the placed in service date for clean-fuel vehicle refueling property by one year. The deduction for clean-fuel vehicle refueling property is available for property placed in service prior to January 1, 2007.

EFFECTIVE DATE

The provision is effective on the date of enactment.

7. Taxable Income Limit on Percentage Depletion for Marginal Production (sec. 307 of the bill and sec. 613A of the Code)

PRESENT LAW

In general

Depletion, like depreciation, is a form of capital cost recovery. In both cases, the taxpayer is allowed a deduction in recognition of the fact that an asset—in the case of depletion for oil or gas interests, the mineral reserve itself—is being expended in order to produce income. Certain costs incurred prior to drilling an oil or gas property are recovered through the depletion deduction. These include costs of acquiring the lease or other interest in the property and geological and geophysical costs (in advance of actual drilling). Depletion is available to any person having an economic interest in a producing property.

Two methods of depletion are allowable under the Code: (1) the cost depletion method, and (2) the percentage depletion method (secs. 611–613). Under the cost depletion method, the taxpayer deducts that portion of the adjusted basis of the depletable property which is equal to the ratio of units sold from that property during the taxable year to the number of units remaining as of the end of taxable year plus the number of units sold during the taxable year. Thus, the amount recovered under cost depletion may never exceed the taxpayer's basis in the property.

Under the percentage depletion method, generally, 15 percent of the taxpayer's gross income from an oil- or gas-producing property is allowed as a deduction in each taxable year (sec. 613A(c)). The amount deducted generally may not exceed 100 percent of the net income from that property in any year (the "net-income limitation") (sec. 613(a)). The Taxpayer Relief Act of 1997 suspended the 100-percent-of-net-income limitation for production from marginal wells for taxable years beginning after December 31, 1997, and before January 1, 2000. The limitation subsequently was extended to include taxable years beginning before January 1, 2002. Additionally, the percentage depletion deduction for all oil and gas properties may not exceed 65 percent of the taxpayer's overall taxable income (determined before such deduction and adjusted for certain loss carrybacks and trust distributions) (sec. 613A(d)(1)).[19] Because percentage depletion, unlike cost depletion, is computed without regard to the taxpayer's basis in the depletable property, cumulative depletion deductions may be greater than the amount expended by the taxpayer to acquire or develop the property.

[19] Amounts disallowed as a result of this rule may be carried forward and deducted in subsequent taxable years, subject to the 65-percent taxable income limitation for those years.

A taxpayer is required to determine the depletion deduction for each oil or gas property under both the percentage depletion method (if the taxpayer is entitled to use this method) and the cost depletion method. If the cost depletion deduction is larger, the taxpayer must utilize that method for the taxable year in question (sec. 613(a)).

Limitation of oil and gas percentage depletion to independent producers and royalty owners

Generally, only independent producers and royalty owners (as contrasted to integrated oil companies) are allowed to claim percentage depletion. Percentage depletion for eligible taxpayers is allowed only with respect to up to 1,000 barrels of average daily production of domestic crude oil or an equivalent amount of domestic natural gas (sec. 613A(c)). For producers of both oil and natural gas, this limitation applies on a combined basis.

In addition to the independent producer and royalty owner exception, certain sales of natural gas under a fixed contract in effect on February 1, 1975, and certain natural gas from geopressured brine, are eligible for percentage depletion, at rates of 22 percent and 10 percent, respectively. These exceptions apply without regard to the 1,000-barrel-per-day limitation and regardless of whether the producer is an independent producer or an integrated oil company.

REASONS FOR CHANGE

The Committee notes that oil is, and will continue to be, vital to the American economy. The Committee believes that extension of the current waiver of the 100-percent-of-income-limit will contribute to investment in domestic oil and gas production.

EXPLANATION OF PROVISION

The provision extends the period when the 100-percent net-income limit is suspended to include taxable years beginning after December 31, 2001 and before January 1, 2004.

EFFECTIVE DATE

The provision is effective on the date of enactment.

8. Extension of Authority to Issue Qualified Zone Academy Bonds (sec. 308 of the bill and sec. 1397E of the Code)

PRESENT LAW

Tax-exempt bonds

Interest on State and local governmental bonds generally is excluded from gross income for Federal income tax purposes if the proceeds of the bonds are used to finance direct activities of these governmental units or if the bonds are repaid with revenues of the governmental units. Activities that can be financed with these tax-exempt bonds include the financing of public schools (sec. 103).

Qualified zone academy bonds

As an alternative to traditional tax-exempt bonds, States and local governments are given the authority to issue "qualified zone academy bonds" ("QZABs") (sec. 1397E). A total of $400 million of

qualified zone academy bonds may be issued annually in calendar years 1998 through 2001. The $400 million aggregate bond cap is allocated each year to the States according to their respective populations of individuals below the poverty line. Each State, in turn, allocates the credit authority to qualified zone academies within such State.

Financial institutions that hold qualified zone academy bonds are entitled to a nonrefundable tax credit in an amount equal to a credit rate multiplied by the face amount of the bond. A taxpayer holding a qualified zone academy bond on the credit allowance date is entitled to a credit. The credit is includable in gross income (as if it were a taxable interest payment on the bond), and may be claimed against regular income tax and AMT liability.

The Treasury Department sets the credit rate at a rate estimated to allow issuance of qualified zone academy bonds without discount and without interest cost to the issuer. The maximum term of the bond is determined by the Treasury Department, so that the present value of the obligation to repay the bond is 50 percent of the face value of the bond.

"Qualified zone academy bonds" are defined as any bond issued by a State or local government, provided that (1) at least 95 percent of the proceeds are used for the purpose of renovating, providing equipment to, developing course materials for use at, or training teachers and other school personnel in a "qualified zone academy" and (2) private entities have promised to contribute to the qualified zone academy certain equipment, technical assistance or training, employee services, or other property or services with a value equal to at least 10 percent of the bond proceeds.

A school is a "qualified zone academy" if (1) the school is a public school that provides education and training below the college level, (2) the school operates a special academic program in cooperation with businesses to enhance the academic curriculum and increase graduation and employment rates, and (3) either (a) the school is located in an empowerment zones enterprise community designated under the Code, or (b) it is reasonably expected that at least 35 percent of the students at the school will be eligible for free or reduced-cost lunches under the school lunch program established under the National School Lunch Act.

REASONS FOR CHANGE

The Committee believes that extension of authority to issue qualified zone academy bonds is appropriate in light of the educational needs that exist today.

EXPLANATION OF PROVISION

The provision authorizes issuance of up to $400 million of qualified zone academy bonds annually in calendar years 2002 and 2003.

EFFECTIVE DATE

The provision is effective on the date of enactment.

9. Extension of Increased Coverover Payments to Puerto Rico and the Virgin Islands (sec. 309 of the bill and sec. 7652 of the Code)

PRESENT LAW

A $13.50 per proof gallon[20] excise tax is imposed on distilled spirits produced in, or imported or brought into, the United States. The excise tax does not apply to distilled spirits that are exported from the United States or to distilled spirits that are consumed in U.S. possessions (e.g., Puerto Rico and the Virgin Islands).

The Code provides for coverover (payment) of $13.25 per proof gallon of the excise tax imposed on rum imported (or brought) into the United States (without regard to the country of origin) to Puerto Rico and the Virgin Islands during the period July 1, 1999 through December 31, 2001. Effective on January 1, 2002, the coverover rate is scheduled to return to its permanent level of $10.50 per proof gallon.

Amounts covered over to Puerto Rico and the Virgin Islands are deposited into the treasuries of the two possessions for use as those possessions determine.

REASONS FOR CHANGE

The Committee believes that extension of the increased coverover rate to Puerto Rico and the Virgin Islands will contribute to economic stability in those possessions.

EXPLANATION OF PROVISION

The provision extends the $13.25-per-proof-gallon coverover rate for two additional years, through December 31, 2003.

The Committee is aware that Puerto Rico currently allocates a portion of the coverover payments it receives to the Puerto Rico Conservation Trust. The Committee believes it is appropriate that this allocation continue through the period when the $13.25-per-proof-gallon rate is extended.

EFFECTIVE DATE

The provision is effective on the date of enactment.

10. Tax on Failure to Comply with Mental Health Parity Requirements (sec. 310 of the bill and sec. 9812 of the Code)

PRIOR LAW

The Mental Health Parity Act of 1996 amended ERISA and the Public Health Service Act to provide that group health plans that provide both medical and surgical benefits and mental health benefits cannot impose aggregate lifetime or annual dollar limits on mental health benefits that are not imposed on substantially all medical and surgical benefits. The provisions of the Mental Health Parity Act are effective with respect to plan years beginning on or after January 1, 1998, but do not apply to benefits for services furnished on or after September 30, 2001.

The Taxpayer Relief Act of 1997 added to the Internal Revenue Code the requirements imposed under the Mental Health Parity

[20] A proof gallon is a liquid gallon consisting of 50 percent alcohol.

Act, and imposed an excise tax on group health plans that fail to meet the requirements. The excise tax is equal to $100 per day during the period of noncompliance and is imposed on the employer sponsoring the plan if the plan fails to meet the requirements. The maximum tax that can be imposed during a taxable year cannot exceed the lesser of 10 percent of the employer's group health plan expenses for the prior year or $500,000. No tax is imposed if the Secretary determines that the employer did not know, and exercising reasonable diligence would not have known, that the failure existed.

The excise tax is applicable with respect to plan years beginning on or after January 1, 1998, and expired with respect to benefits for services provided on or after September 30, 2001.

REASONS FOR CHANGE

The Committee believes it appropriate to provide an extension of the mental health parity provisions.

EXPLANATION OF PROVISION

The excise tax on failures to comply with mental health parity requirements is extended for two years.

EFFECTIVE DATE

The provision is effective with respect to plan years beginning on or after January 1, 2002, and would not apply to benefits for services furnished on or after January 1, 2004.

11. Delay in Effective Date of Requirement for Approved Diesel or Kerosene Terminal (sec. 311 of the bill and sec. 4101 of the Code)

PRESENT LAW

Excise taxes are imposed on highway motor fuels, including gasoline, diesel fuel, and kerosene, to finance the Highway Trust Fund programs. Subject to limited exceptions, these taxes are imposed on all such fuels when they are removed from registered pipeline or barge terminal facilities, with any tax-exemptions being accomplished by means of refunds to consumers of the fuel.[21] One such exception allows removal of diesel fuel or kerosene without payment of tax if the fuel is destined for a nontaxable use (e.g., use as heating oil) and is indelibly dyed.

Terminal facilities are not permitted to receive and store non-tax-paid motor fuels unless they are registered with the Internal Revenue Service. Under present law, a prerequisite to registration is that if the terminal offers for sale diesel fuel, it must offer both dyed and undyed diesel fuel. Similarly, if the terminal offers for sale kerosene, it must offer both dyed and undyed kerosene. This "dyed-fuel mandate" was enacted in 1997, to be effective on July 1, 1998. Subsequently, the effective date was delayed until July 1, 2000, and later until January 1, 2002.

[21] Tax is imposed before that point if the motor fuel is transferred (other than in bulk) from a refinery or if the fuel is sold to an unregistered party while still held in the refinery or bulk distribution system (e.g., in a pipeline or terminal facility).

REASONS FOR CHANGE

When the rules governing taxation of kerosene used as a highway motor fuel were enacted in 1997, the Congress was concerned that dyed kerosene and diesel fuel (destined for nontaxable uses) might be unavailable in markets where those fuels were commonly used (e.g., as heating oil). To ensure availability of untaxed, dyed fuels for those uses, the Congress included a requirement that terminals offer both dyed and undyed kerosene and diesel fuel (if they offered the fuels for sale at all) as a condition of receiving untaxed fuels. Since that time, markets have provided dyed kerosene and diesel fuel for nontaxable uses where there is a demand for them. The Committee believes a further delay in this registration requirement is appropriate to allow a more complete evaluation of whether the requirement should be repealed or implemented.

EXPLANATION OF PROVISION

The effective date of the diesel fuel and kerosene dyeing mandate is delayed for two additional years, until January 1, 2004.

EFFECTIVE DATE

The provision is effective on the date of enactment.

B. One-Year Extension of Provision Expiring in 2002

1. Extension of Archer Medical Savings Accounts ("MSAs") (sec. 321 of the bill and sec. 220 of the Code)

PRESENT LAW

In general

Within limits, contributions to an Archer medical savings account ("MSA") are deductible in determining adjusted gross income if made by an eligible individual and are excludable from gross income and wages for employment tax purposes if made by the employer of an eligible individual. Earnings on amounts in an Archer MSA are not currently taxable. Distributions from an Archer MSA for medical expenses are not taxable. Distributions not used for medical expenses are taxable. In addition, distributions not used for medical expenses are subject to an additional 15-percent tax unless the distribution is made after age 65, death, or disability.

Eligible individuals

Archer MSAs are available to employees covered under an employer-sponsored high deductible plan of a small employer and self-employed individuals covered under a high deductible health plan.[22] An employer is a small employer if it employed, on average, no more than 50 employees on business days during either the preceding or the second preceding year. An individual is not eligible for an Archer MSA if they are covered under any other health plan in addition to the high deductible plan.

[22] Self-employed individuals include more than 2-percent shareholders of S corporations who are treated as partners for purposes of fringe benefit rules pursuant to section 1372.

Tax treatment of and limits on contributions

Individual contributions to an Archer MSA are deductible (within limits) in determining adjusted gross income (i.e., "above the line"). In addition, employer contributions are excludable from gross income and wages for employment tax purposes (within the same limits), except that this exclusion does not apply to contributions made through a cafeteria plan. In the case of an employee, contributions can be made to an Archer MSA either by the individual or by the individual's employer.

The maximum annual contribution that can be made to an Archer MSA for a year is 65 percent of the deductible under the high deductible plan in the case of individual coverage and 75 percent of the deductible in the case of family coverage.

Definition of high deductible plan

A high deductible plan is a health plan with an annual deductible of at least $1,600 and no more than $2,400 in the case of individual coverage and at least $3,200 and no more than $4,800 in the case of family coverage. In addition, the maximum out-of-pocket expenses with respect to allowed costs (including the deductible) must be no more than $3,200 in the case of individual coverage and no more than $5,850 in the case of family coverage.[23] A plan does not fail to qualify as a high deductible plan merely because it does not have a deductible for preventive care as required by State law. A plan does not qualify as a high deductible health plan if substantially all of the coverage under the plan is for permitted coverage (as described above). In the case of a self-insured plan, the plan must in fact be insurance (e.g., there must be appropriate risk shifting) and not merely a reimbursement arrangement.

Taxation of distributions

Distributions from an Archer MSA for the medical expenses of the individual and his or her spouse or dependents generally are excludable from income.[24] However, in any year for which a contribution is made to an Archer MSA, withdrawals from an Archer MSA maintained by that individual generally are excludable from income only if the individual for whom the expenses were incurred was covered under a high deductible plan for the month in which the expenses were incurred.[25] For this purpose, medical expenses are defined as under the itemized deduction for medical expenses, except that medical expenses do not include expenses for insurance other than long-term care insurance, premiums for health care continuation coverage, and premiums for health care coverage while an individual is receiving unemployment compensation under Federal or State law.

Distributions that are not used for medical expenses are includible in income. Such distributions are also subject to an additional 15-percent tax unless made after age 65, death, or disability.

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[23] These dollar amounts are for 2001. These amounts are indexed for inflation in $50 increments.

[24] This exclusion does not apply to expenses that are reimbursed by insurance or otherwise.

[25] The exclusion still applies to expenses for continuation coverage or coverage while the individual is receiving unemployment compensation, even for an individual who is not an eligible individual.

Cap on taxpayers utilizing Archer MSAs

The number of taxpayers benefiting annually from an Archer MSA contribution is limited to a threshold level (generally 750,000 taxpayers). If it is determined in a year that the threshold level has been exceeded (called a "cut-off" year) then, in general, for succeeding years during the pilot period 1997–2002, only those individuals who (1) made an Archer MSA contribution or had an employer Archer MSA contribution for the year or a preceding year (i.e., are active Archer MSA participants) or (2) are employed by a participating employer, those individuals are eligible for an Archer MSA contribution. In determining whether the threshold for any year has been exceeded, Archer MSAs of individuals who were not covered under a health insurance plan for the six month period ending on the date on which coverage under a high deductible plan commences would not be taken into account.[26] However, if the threshold level is exceeded in a year, previously uninsured individuals are subject to the same restriction on contributions in succeeding years as other individuals. That is, they would not be eligible for an Archer MSA contribution for a year following a cut-off year unless they are an active Archer MSA participant (i.e., had an Archer MSA contribution for the year or a preceding year) or are employed by a participating employer.

The number of Archer MSAs established has not exceeded the threshold level.

End of Archer MSA pilot program

After 2002, no new contributions may be made to Archer MSAs except by or on behalf of individuals who previously had Archer MSA contributions and employees who are employed by a participating employer. An employer is a participating employer if (1) the employer made any Archer MSA contributions for any year to an Archer MSA on behalf of employees or (2) at least 20 percent of the employees covered under a high deductible plan made Archer MSA contributions of at least $100 in the year 2001.

Self-employed individuals who made contributions to an Archer MSA during the period 1997–2002 also may continue to make contributions after 2002.

REASONS FOR CHANGE

Archer MSAs were enacted to provide additional health insurance options and to give individuals more control over their health care dollars by providing incentives for individuals to be more cost conscious consumers of health care. The Committee believes that an extension of the Archer MSA program is appropriate in order to continue to pursue such objectives.

EXPLANATION OF PROVISION

The provision extends the Archer MSA program for another year, through December 31, 2003.

[26] Permitted coverage, as described above, does not constitute coverage under a health insurance plan for this purpose.

EFFECTIVE DATE

The provision is effective on the date of enactment.

C. Permanent Extension

1. Extend Exceptions under Subpart F for Active Financing Income (sec. 331 of the bill and secs. 953 and 954 of the Code)

PRESENT LAW

Under the subpart F rules, 10-percent U.S. shareholders of a controlled foreign corporation ("CFC") are subject to U.S. tax currently on certain income earned by the CFC, whether or not such income is distributed to the shareholders. The income subject to current inclusion under the subpart F rules includes, among other things, foreign personal holding company income and insurance income. In addition, 10-percent U.S. shareholders of a CFC are subject to current inclusion with respect to their shares of the CFC's foreign base company services income (i.e., income derived from services performed for a related person outside the country in which the CFC is organized).

Foreign personal holding company income generally consists of the following: (1) dividends, interest, royalties, rents, and annuities; (2) net gains from the sale or exchange of (a) property that gives rise to the preceding types of income, (b) property that does not give rise to income, and (c) interests in trusts, partnerships, and REMICs; (3) net gains from commodities transactions; (4) net gains from foreign currency transactions; (5) income that is equivalent to interest; (6) income from notional principal contracts; and (7) payments in lieu of dividends.

Insurance income subject to current inclusion under the subpart F rules includes any income of a CFC attributable to the issuing or reinsuring of any insurance or annuity contract in connection with risks located in a country other than the CFC's country of organization. Subpart F insurance income also includes income attributable to an insurance contract in connection with risks located within the CFC's country of organization, as the result of an arrangement under which another corporation receives a substantially equal amount of consideration for insurance of other country risks. Investment income of a CFC that is allocable to any insurance or annuity contract related to risks located outside the CFC's country of organization is taxable as subpart F insurance income (Prop. Treas. Reg. sec. 1.953–1(a)).

Temporary exceptions from foreign personal holding company income, foreign base company services income, and insurance income apply for subpart F purposes for certain income that is derived in the active conduct of a banking, financing, or similar business, or in the conduct of an insurance business (so-called "active financing income").[27]

With respect to income derived in the active conduct of a banking, financing, or similar business, a CFC is required to be pre-

[27] Temporary exceptions from the subpart F provisions for certain active financing income applied only for taxable years beginning in 1998. Those exceptions were modified and extended for one year, applicable only for taxable years beginning in 1999. The Tax Relief Extension Act of 1999 (P.L. No. 106–170) clarified and extended the temporary exceptions for two years, applicable only for taxable years beginning after 1999 and before 2002.

dominantly engaged in such business and to conduct substantial activity with respect to such business in order to qualify for the exceptions. In addition, certain nexus requirements apply, which provide that income derived by a CFC or a qualified business unit ("QBU") of a CFC from transactions with customers is eligible for the exceptions if, among other things, substantially all of the activities in connection with such transactions are conducted directly by the CFC or QBU in its home country, and such income is treated as earned by the CFC or QBU in its home country for purposes of such country's tax laws. Moreover, the exceptions apply to income derived from certain cross border transactions, provided that certain requirements are met. Additional exceptions from foreign personal holding company income apply for certain income derived by a securities dealer within the meaning of section 475 and for gain from the sale of active financing assets.

In the case of insurance, in addition to a temporary exception from foreign personal holding company income for certain income of a qualifying insurance company with respect to risks located within the CFC's country of creation or organization, certain temporary exceptions from insurance income and from foreign personal holding company income apply for certain income of a qualifying branch of a qualifying insurance company with respect to risks located within the home country of the branch, provided certain requirements are met under each of the exceptions. Further, additional temporary exceptions from insurance income and from foreign personal holding company income apply for certain income of certain CFCs or branches with respect to risks located in a country other than the United States, provided that the requirements for these exceptions are met.

In the case of a life insurance or annuity contract, reserves for such contracts are determined as follows for purposes of these provisions. The reserves equal the greater of: (1) the net surrender value of the contract (as defined in sec. 807(e)(1)(A)), including in the case of pension plan contracts; or (2) the amount determined by applying the tax reserve method that would apply if the qualifying life insurance company were subject to tax under Subchapter L of the Code, with the following modifications. First, there is substituted for the applicable Federal interest rate an interest rate determined for the functional currency of the qualifying insurance company's home country, calculated (except as provided by the Treasury Secretary in order to address insufficient data and similar problems) in the same manner as the mid-term applicable Federal interest rate (within the meaning of sec. 1274(d)). Second, there is substituted for the prevailing State assumed rate the highest assumed interest rate permitted to be used for purposes of determining statement reserves in the foreign country for the contract. Third, in lieu of U.S. mortality and morbidity tables, mortality and morbidity tables are applied that reasonably reflect the current mortality and morbidity risks in the foreign country. Fourth, the Treasury Secretary may provide that the interest rate and mortality and morbidity tables of a qualifying insurance company may be used for one or more of its branches when appropriate. In no event may the reserve for any contract at any time exceed the foreign statement reserve for the contract, reduced by

any catastrophe, equalization, or deficiency reserve or any similar reserve.

Present law also provides a temporary exception from foreign personal holding company income for income from investment of assets equal to 10 percent of reserves (determined for purposes of the provision) for contracts regulated in the country in which sold as life insurance or annuity contracts. This exception does not apply to investment income with respect to excess surplus.

REASONS FOR CHANGE

In the Taxpayer Relief Act of 1997, one-year temporary exceptions from foreign personal holding company income were enacted for income from the active conduct of an insurance, banking, financing, or similar business.[28] In the Tax and Trade Relief Extension Act of 1998, the Congress extended the temporary exceptions for an additional year, with certain modifications designed to treat various types of businesses with active financing income more similarly to each other than did the 1997 provision.[29] In the Tax Relief Extension Act of 1999, Congress extended the temporary extensions for an additional two years, as modified by the 1998 Act, and with a clarification relating to the application of prior law in the event of future non-application of the temporary provisions.[30] The Committee believes that it is appropriate to permanently extend the temporary provisions, as modified by the previous legislation, with an additional modification relating to the determination of certain reserves for life insurance and annuity contracts. The Committee believes that the use of foreign statement reserves for exempt life insurance and annuity contracts may be appropriate under these exceptions in certain circumstances, provided IRS approval is obtained, based on whether such use with respect to those foreign contracts provides an appropriate means of measuring income for Federal income tax purposes.

EXPLANATION OF PROVISION

The provision extends permanently the present-law temporary exceptions from subpart F foreign personal holding company income, foreign base company services income, and insurance income for certain income that is derived in the active conduct of a banking, financing, or similar business, or in the conduct of an insurance business.

The provision generally retains present law with respect to the determination of an insurance company's reserve for a life insurance or annuity contract under these exceptions. The provision does, however, permit a taxpayer in certain circumstances, subject to approval by the IRS through the ruling process, to establish that the reserve for such contracts is the amount taken into account in determining the foreign statement reserve for the contract (reduced by catastrophe, equalization, or deficiency reserve or any similar reserve). IRS approval is to be based on whether the method, the

[28] The President canceled this provision in 1997 pursuant to the Line Item Veto Act. On June 25, 1998, the U.S. Supreme Court held that the cancellation procedures set forth in the Line Item Veto Act are unconstitutional. *Clinton* v. *City of New York,* 524 U.S. 417 (1998).

[29] The Tax and Trade Relief Extension Act of 1998, Division J, Making Omnibus Consolidated and Emergency Supplemental Appropriations for Fiscal Year 1999, P.L. No. 105–277, sec. 1005 (1998).

[30] The Tax Relief Extension Act of 1999, P.L. No. 106–170, sec. 503 (1999).

interest rate, the mortality and morbidity assumptions, and any other factors taken into account in determining foreign statement reserves (taken together or separately) provide an appropriate means of measuring income for Federal income tax purposes. In seeking a ruling, the taxpayer is required to provide the IRS with necessary and appropriate information as to the method, interest rate, mortality and morbidity assumptions and other assumptions under the foreign reserve rules so that a comparison can be made to the reserve amount determined by applying the tax reserve method that would apply if the qualifying insurance company were subject to tax under Subchapter L of the Code (with the modifications provided under present law for purposes of these exceptions). Present law continues to apply with respect to reserves for any life insurance or annuity contract for which the IRS has not approved the use of the foreign statement reserve. An IRS ruling request under this provision is subject to the present-law provisions relating to IRS user fees.

EFFECTIVE DATE

The provision is effective for taxable years of foreign corporations beginning after December 31, 2001, and for taxable years of U.S. shareholders with or within which such taxable years of such foreign corporations end.

D. Other Provisions

1. Discharge of Indebtedness of an S Corporation (sec. 341 of the bill and sec. 108 of the Code)

PRESENT LAW

In general, an S corporation is not subject to the corporate income tax on its items of income and loss. Instead, an S corporation passes through its items of income and loss to its shareholders. Each shareholder takes into account separately his or her pro rata share of these items on their individual income tax returns. To prevent double taxation of these items, each shareholder's basis in the stock of the S corporation is increased by the amount included in income (including tax-exempt income) and is decreased by the amount of any losses (including nondeductible losses) taken into account. A shareholder may deduct losses only to the extent of a shareholder's basis in his or her stock in the S corporation plus the shareholder's adjusted basis in any indebtedness of the corporation to the shareholder. Any loss that is disallowed by reason of lack of basis is "suspended" at the corporate level and is carried forward and allowed in any subsequent year in which the shareholder has adequate basis in the stock or debt.

In general, gross income includes income from the discharge of indebtedness. However, income from the discharge of indebtedness of a taxpayer in a bankruptcy case or when the taxpayer is insolvent (to the extent of the insolvency) is excluded from income.[31] The taxpayer is required to reduce tax attributes, such as net operating losses, certain carryovers, and basis in assets, to the extent of the excluded income.

[31] Special rules also apply to certain real estate debt and farm debt.

In the case of an S corporation, the eligibility for the exclusion and the attribute reduction are applied at the corporate level. For this purpose, a shareholder's suspended loss is treated as a tax attribute that is reduced. Thus, if the S corporation is in bankruptcy or is insolvent, any income from the discharge of indebtedness by a creditor of the S corporation is excluded from the corporation's income, and the S corporation reduces its tax attributes (including any suspended losses).

To illustrate these rules, assume that a sole shareholder of an S corporation has zero basis in its stock of the corporation. The S corporation borrows $100 from a third party and loses the entire $100. Because the shareholder has no basis in its stock, the $100 loss is "suspended" at the corporate level. If the $100 debt is forgiven when the corporation is in bankruptcy or is insolvent, the $100 income from the discharge of indebtedness is excluded from income, and the $100 "suspended" loss should be eliminated in order to achieve a tax result that is consistent with the economics of the transactions in that the shareholder has no economic gain or loss from these transactions.

Notwithstanding the economics of the overall transaction, the United States Supreme Court ruled in the case of *Gitlitz* v. *Commissioner*[32] that, under present law, income from the discharge of indebtedness of an S corporation that is excluded from income is treated as an item of income which increases the basis of a shareholder's stock in the S corporation and allows the suspended corporate loss to pass thru to a shareholder. Thus, under the decision, an S corporation shareholder is allowed to deduct a loss for tax purposes that it did not economically incur.

REASONS FOR CHANGE

The Committee believes that it is inappropriate for a shareholder of an insolvent or bankrupt S corporation to take into account excluded income from the discharge of the S corporation's indebtedness and thereby increase the shareholder's adjusted basis in the stock. Under the provisions of the Code, an increase in the stock basis allows the shareholder a deduction for an amount of loss that is not economically borne by the shareholder.

As a general matter, the Committee believes that where, as in the case of the present statute under section 108, the plain text of a provision of the Internal Revenue Code produces an ambiguity, the provision should be read as closing, not maintaining, a loophole that would result in an inappropriate reduction of tax liability.

EXPLANATION OF PROVISION

The provision provides that income from the discharge of indebtedness of an S corporation that is excluded from the S corporation's income is not taken into account as an item of income by any shareholder and thus does not increase the basis of any shareholder's stock in the corporation.

EFFECTIVE DATE

The provision applies to discharges of indebtedness after October 11, 2001.

[32] 531 U.S. 206 (2001).

2. Limitation on Use of Non-Accrual Experience Method of Accounting (sec. 342 of the bill and sec. 448 of the Code)

PRESENT LAW

An accrual method taxpayer generally must recognize income when all the events have occurred that fix the right to receive the income and the amount of the income can be determined with reasonable accuracy. An accrual method taxpayer may deduct the amount of any receivable that was previously included in income that becomes worthless during the year.

Accrual method taxpayers are not required to include in income amounts to be received for the performance of services which, on the basis of experience, will not be collected (the "non-accrual experience method"). The availability of this method is conditioned on the taxpayer not charging interest or a penalty for failure to timely pay the amount charged.

Generally, a cash method taxpayer is not required to include an amount in income until received. A taxpayer generally may not use the cash method if purchase, production, or sale of merchandise is an income producing factor. Such taxpayers generally are required to keep inventories and use an accrual method of accounting. In addition, corporations (and partnerships with corporate partners) generally may not use the cash method of accounting if their average annual gross receipts years exceed $5 million. An exception to this $5 million rule is provided for qualified personal service corporations. A qualified personal service corporation is a corporation (1) substantially all of whose activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts or consulting and (2) substantially all of the stock of which is owned by current or former employees performing such services, their estates or heirs. Qualified personal service corporations are allowed to use the cash method without regard to whether their average annual gross receipts exceed $5 million.

REASONS FOR CHANGE

The Committee understands that the use of the non-accrual experience method provides the equivalent of a bad debt reserve, which generally is not available to taxpayers using an accrual method of accounting. The Committee believes that accrual method taxpayers should be treated similarly, unless there is a strong indication that different treatment is necessary to clearly reflect income or to address a particular competitive situation.

The Committee understands that accrual basis providers of qualified services (services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts or consulting) compete on a regular basis with competitors using the cash method of accounting. The Committee believes that this competitive situation justifies the continued availability of the non- accrual experience method with respect to amounts due to be received for the performance of qualified services. The Committee believes that it is important to avoid the disparity of treatment between competing cash and accrual method providers of qualified services that could result if the non-accrual experience method were eliminated with regard to amounts to be received for such services.

The Committee also recognizes the burdens placed on small businesses to comply with the complexity of the federal income tax code and, in this time of economic uncertainty, the importance of cash flow to small businesses. As such, the Committee believes that small business service providers using an accrual method of accounting should be permitted to continue to use the non-accrual experience method.

In addition, the Committee believes that the formula contained in Temp. Reg. section 1.448–2T may not clearly reflect the amount of income that, based on experience, will not be collected for many qualified services providers, especially for those where significant time elapses between the rendering of the service and a final determination that the account will not be collected. Providers of qualified services should not be subject to a formula that requires the payments of taxes on receivables that will not be collected.

EXPLANATION OF PROVISION

Under the provision, the non-accrual experience method of accounting is available only for amounts to be received for the performance of qualified services and for services provided by certain small businesses. Amounts to be received for all other services are subject to the general rule regarding inclusion in income. Qualified services are services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts or consulting. As under present law, the availability of this method is conditioned on the taxpayer not charging interest or a penalty for failure to timely pay the amount charged.

Under a special rule, the non-accrual experience method of accounting continues to be available for the performance of non-qualified services if the average annual gross receipts (as defined in sec. 448(c)) of the taxpayer (or any predecessor) does not exceed $5 million. The rules of paragraph (2) and (3) of section 448(c) (i.e., the rules regarding the aggregation of related taxpayers, taxpayers not in existence for the entire three year period, short taxable years, definition of gross receipts, and treatment of predecessors) apply for purposes of determining the average annual gross receipts test.

The provision requires that the Secretary of the Treasury prescribe regulations to permit a taxpayer to use alternative computations or formulas if such alternative computations or formulas accurately reflect, based on experience, the amount of its year-end receivables that will not be collected. It is anticipated that the Secretary of the Treasury will consider providing safe harbors in such regulations that may be relied upon by taxpayers. In addition, the provision also provides that the Secretary of the Treasury permit taxpayers to adopt, or request consent of the Secretary of the Treasury to change to, an alternative computation or formula that clearly reflects the taxpayer's experience. The provision requires the Secretary of Treasury to approve a request provided that the alternative computation or formula clearly reflects the taxpayer's experience.

EFFECTIVE DATE

The provision is effective for taxable years ending after date of enactment. Any change in the taxpayer's method of accounting required as a result of the limitation on the use of the non-accrual

experience method is treated as a voluntary change initiated by the taxpayer with the consent of the Secretary of the Treasury. Any resultant section 481(a) adjustment is to be taken into account over a period not to exceed the lesser of the number of years the taxpayer has used the non-accrual experience method of accounting or four years under principles consistent with those in Rev. Proc. 99–49.[33]

TITLE IV—SUPPLEMENTAL REBATE; OTHER PROVISIONS

A. Supplemental Rebate (Sec. 401 of the Bill and Sec. 6428 of the Code)

PRESENT LAW

The Economic Growth and Tax Relief Reconciliation Act of 2001 provided for a rate reduction credit for 2001. The credit is computed in the following manner. Taxpayers would be entitled to a credit in tax year 2001 of 5 percent (the difference between the 15-percent rate and the 10-percent rate) of the amount of income that would have been eligible for the new 10-percent rate. Taxpayers may not receive this credit in excess of their income tax liability (determined after nonrefundable credits).

Most eligible taxpayers have received this credit in the form of a check issued by the Department of the Treasury. The amount of the check was computed in the same manner as the credit, except that it was done on the basis of tax returns filed for 2000 (instead of 2001).

On their tax returns for 2001, taxpayers will reconcile the amount of the credit with the check they receive in the following manner. They will complete a worksheet calculating the amount of the credit based on their 2001 tax return. They will then subtract from the credit the amount of the check they received. For many taxpayers, these two amounts would be the same. If, however, the result is a positive number (because, for example, the taxpayer paid no tax in 2000 but is paying tax in 2001), the taxpayer may claim that amount as a credit against 2001 tax liability. If, however, the result is negative (because, for example, the taxpayer paid tax in 2000 but owes no tax for 2001), the taxpayer is not required to repay that amount to the Treasury. Otherwise, the checks have no effect on tax returns filed in 2001; the amount is not includible in gross income and it does not otherwise reduce the amount of withholding. In no event may the Department of the Treasury issue checks after December 31, 2001. This is designed to prevent errors by taxpayers who might claim the full amount of the credit on their 2001 tax returns and file those returns early in 2002, at the same time the Treasury check might be mailed to them. Payment of the credit (or the check) is treated, for all purposes of the Code,[34] as a payment of tax. As such, the credit or the check is subject to the refund offset provisions, such as those applicable to past-due child support under section 6402 of the Code.

In general, taxpayers eligible for the credit (and the check) are individuals other than estates or trusts, nonresident aliens, or de-

[33] 1999–2C.B. 725

[34] A special rule provides that no interest will be paid with respect to the checks.

pendents. The determination of this status for the relevant year is made on the basis of the information filed on the tax return.

REASONS FOR CHANGE

The Committee believes that providing supplemental rebates will provide further stimulus to the economy.

EXPLANATION OF PROVISION

The bill provides a new supplemental rebate. Individuals who filed income tax returns for 2000[35] (regardless of whether they had any income tax liability or any payroll tax liability) are eligible for this supplemental rebate. The amount of the rebate is calculated in the following manner: taxpayers are eligible for the maximum rebate amount for their filing status ($300 single or married filing separately, $500 head of household, $600 joint filers) minus the amount (if any) of any previous rebate check issued. Thus, if a single person received $100 earlier this year as her rate reduction credit, she will receive an additional $200. Those who earlier received the full amounts for their filing status will receive nothing additional. It is irrelevant whether the taxpayer showed any amount as wages on the 2000 income tax return.

Dependents and nonresident aliens are ineligible for these supplemental rebates (as they were for the previous rebates). The Committee expects that the IRS will send notices to affected taxpayers explaining the computation of their supplemental rebate amounts and how the taxpayer should properly complete the rebate reconciliation schedule contained in the tax return forms package.

EFFECTIVE DATE

The provision is effective on the date of enactment. In order to prevent difficulties that could arise in the simultaneous administration of two rebate provisions, the issuance of checks under the previous rebate provision must cease on the date of enactment of these supplemental rebates.

B. Special Reed Act Transfer in Fiscal Year 2002 (sec. 402 of the bill)

1. Repeal of Certain Provisions Added by the Balanced Budget Act of 1997

PRESENT LAW

When three Federal accounts in the Unemployment Trust Fund (UTF) reach their statutory limits at the end of a Federal fiscal year, any excess funds are transferred to the individual State accounts in the UTF. These transfers are called "Reed Act" distributions. States can use this funding for payment of cash benefits and administrating their unemployment compensation and employment services programs. The Balanced Budget Act of 1997 limited Reed Act transfers to States to $100 million after each of fiscal years

[35] Taxpayers who did not file an income tax return for 2000 but who do file an income tax return for 2001 will continue to be eligible for the rate reduction credit previously enacted, the amount of which is dependent upon the amount of income subject to the 10-percent rate. They are not, however, eligible for this supplemental rebate.

1999, 2000, and 2001 and limited these funds' use to paying administrative expenses of unemployment compensation laws.

REASONS FOR CHANGE

The amount of excess Federal funds in the UTF as of the end of fiscal year 2001 was over $9.3 billion. Under current law, at the beginning of fiscal year 2002, $100 million was transferred to States under the special distribution provision under the Balanced Budget Act of 1997. The additional $9.2 billion in excess funds remained in a Federal unemployment account. Repeal of the special distribution limitation, as provided under the Chairman's amendment, would result in the transfer of the remaining $9.2 billion in excess Federal funds to State accounts.

This distribution will provide States with significant additional funds to address unemployment benefit needs. Funds will be directly transferred into State unemployment accounts, where they will be immediately available to support regular unemployment benefit payments as needed. As provided below, States also may use these new funds for additional unemployment program purposes such as providing extended benefits through the passage of separate State legislation.

EXPLANATION OF PROVISION

The $100 million limit on distributions from excess Federal funds available at the end of fiscal year 2001 is repealed. The provision also repeals the limitation on the use of funds applied to the $100 million special distribution under the Balanced Budget Act of 1997. This limitation applied only to special distributions at the end of fiscal years 1999, 2000, and 2001, and with the repeal of the underlying special distribution provision is no longer relevant.

2. Special Transfer in Fiscal Year 2002

PRESENT LAW

No provision.

REASON FOR CHANGE

Because of limitations imposed by the Balanced Budget Act of 1997, regular Reed Act distributions have not been transferred to States following fiscal years 1999, 2000 and 2001. Instead, transfers were limited to a "special distribution" of $100 million per year at the beginning of each of the subsequent fiscal years, including fiscal year 2002. The result has been a significant accumulation of excess funds in Federal accounts. Absent changes such as those proposed in H.R. 3090, these excess funds will remain in Federal accounts until regular Reed Act transfers resume at the beginning of fiscal year 2003 (on or about October 1, 2002).

The purpose of Section 402 is to accelerate the transfer of surplus Federal unemployment funds for States to use in supporting unemployment benefits and services to help individuals return to work. Federal unemployment accounts, with balances totaling $39 billion at the end of fiscal year 2001, are more than sufficient to support current Federal administrative and other responsibilities under the Federal-State unemployment compensation system. Forwarding Federal surplus funds will provide immediate assistance

to States—especially those with low account balances—to support rising benefit needs as well as demand for extended benefits, additional employment services, and other supports.

H.R. 3090 is consistent with the operation of the Federal-State unemployment compensation program dating to the 1950s, the Committee's longstanding interest in promoting State flexibility and control in deciding how best to support benefit needs, and the need to maintain fiscal responsibility.

As described above, Reed Act distributions have occurred in various fiscal years dating to the 1950s. The 1997 Balanced Budget Act provision created special conditions under which full Reed Act transfers have not been transferred to State accounts in recent years. H.R. 3090 restores the longstanding policy of providing full Reed Act transfers to State accounts, effective immediately (rather than as of the start of fiscal year 2003 as under current law).

Starting with the 1996 Welfare Reform Law (P.L. 104–193, the Personal and Work Opportunity Reconciliation Act of 1996), the Committee has advanced legislation encouraging greater State flexibility and responsibility over cash welfare, child care, child protection and related programs. This goal is consistent with the nation's Federal-State unemployment compensation program, under which States generally determine benefit eligibility and amounts; States also set and collect State unemployment taxes used to support regular unemployment compensation benefits and the State half of the Federal-State extended benefits program. H.R. 3090 promotes State discretion in determining benefit eligibility and amounts by both providing States additional resources and broad discretion in determining how best to use the added Federal funds.

For example, some States with low current account balances may use the added Federal funds to support the payment of regular unemployment benefits, which would require no new State legislation. Depending on State laws and prior account balances, the added funds may allow States to provide regular benefits for additional claimants without raising State taxes or borrowing from the Federal loan account. Based on fiscal year 2001 benefit payment and recipient data, between 2 million and 3 million additional unemployed workers could be provided regular benefits based on the $9 billion in additional Federal funds.

Other States may choose to provide new benefits, for example extended benefits for individuals who have exhausted their regular 26 weeks of benefits. On October 4, 2001, President Bush proposed providing an additional 13 weeks of emergency extended benefits for individuals in States that include a major disaster area or in which unemployment has increased by 30 percent or more in the wake of the September 11 attacks. Section 402 provides States with the funds and flexibility to offer such benefits.

Some States may need additional resources to provide employment services to assist unemployed individuals in returning to work or to process additional unemployment claims. Section 402 allows States to use transferred amounts to support such program purposes as well. It is noteworthy that in recent years States have received far less in Federal funds to assist in administering the unemployment compensation program than employers paid in Federal taxes to support such purposes. The Ways and Means Subcommittee on Human Resources has held a number of hearings in

recent years on the administrative financing of the unemployment program (Unemployment Compensation and the Family and Medical Leave Act, March 9, 2001; Unemployment Compensation Reform, February 29, 2001; Unemployment Compensation, September 7, 2000; HR 3684, the "Employment Security Financing Act of 1998," June 23, 1998; and Unemployment Insurance Issues, April 24, 1997). While falling short of broader administrative financing reforms in which the Committee remains interested, Section 402 provides States broad discretion and immediate Federal funds States may use to address employment service and administrative financing needs.

Section 402 provides the above funding and flexibility while maintaining the interest of the Committee and the Congress in fiscal discipline. According to the Congressional Budget Office, Section 402 results in no increase in the deficit or decrease in the surplus over 10 years. By accelerating future Reed Act distributions into fiscal year 2002, the proposal provides significant immediate assistance to States to support benefit and other program needs. Transfers provided in 2002 are offset by reductions in future transfers, among other program interactions.

The Committee notes that the National Governors Association (NGA) has requested passage of this provision. A letter dated October 4, 2001 signed by Governors Don Sundquist of Tennessee and Frank O'Bannon of Indiana, the Chairman and Vice Chairman, respectively, of NGA's Committee on Human Resources, called for Congress to "amend the Social Security Act to accelerate distribution to state accounts of the excess funds (as defined in the Reed Act) being held in the federal Unemployment Trust Fund."

EXPLANATION OF PROVISION

The Secretary of the Treasury will transfer excess Federal UTF balances as of the close of fiscal year 2001 into the account of each State in the UTF. Each State's share of distributions from the $100 million already provided at the beginning of fiscal year 2002 will be subtracted from the distribution to each State under this provision. (Thus of the $9.3 billion in excess Federal funds as of the end of fiscal year 2001, only $9.2 billion will be provided under H.R. 3090, reflecting the fact that $0.1 billion already has been forwarded to State accounts under the 1997 Balanced Budget Act provision.)

Except as provided below, amounts transferred to State accounts may be used only in the payment of cash benefits to individuals with respect to unemployment under the following conditions:

(1) At the option of the State, cash benefits may include regular unemployment compensation or additions to regular benefits. However, if additions to regular benefits are provided, any additional amounts are to be disregarded in determining any subsequently-provided extended benefits to such individual; and

(2) At the option of the State, cash benefits may be provided to individuals not otherwise eligible for regular unemployment compensation benefits under the laws of the State. Such benefits may include "emergency" extended benefits or other benefit expansions. Benefits to an individual under this condition may not exceed the maximum amount of regular compensation

available under State law for the same period, plus any added benefits provided under (1) above.

Under either condition (1) or (2), amounts transferred may be used in the payment of cash benefits to individuals only for weeks of unemployment beginning after the date of enactment and ending on or before March 11, 2003 (i.e. within 18 months following the September 11, 2001 attacks).

Other than for cash benefits, States may use amounts transferred to their accounts in the administration of their public employment laws and public employment offices, including for the provision of employment services needed to help individuals return to work.

Transfers to State accounts are to be made by the Secretary of Labor no later than 10 days after enactment.

3. Limitations on Transfers

PRESENT LAW

If the Secretary finds that a State is not eligible to receive Reed Act transfers at the beginning of a fiscal year, the amount available for transfer to the State instead is transferred to the Federal unemployment account. If the State becomes eligible during the following one year period, the amount which was available for transfer will be transferred from the Federal unemployment account to the State's account. If the State does not become eligible within one year, the amount remains in the Federal unemployment account for other uses. If any State has borrowed from the Federal unemployment account, any amount that would be transferred is retained and credited against any balance due of the State.

REASONS FOR CHANGE

Funds should be transferred only to States operating unemployment compensation programs that meet Federal requirements. This provision ensures that the special transfers in fiscal year 2002 also will meet these requirements.

EXPLANATION OF PROVISION

This provision applies the same conditions on the timing and limitations on Reed Act transfers under current law to the special transfers that would occur in fiscal year 2002 under the Committee legislation.

4. Technical Amendments

PRESENT LAW

No provision.

REASONS FOR CHANGE

Technical and conforming changes consistent with changes described above.

EXPLANATION OF PROVISION

Makes conforming and technical amendments related to the use of funds in State unemployment accounts for expenses incurred by

States for administration of their unemployment compensation laws and public employment offices.

5. Regulations

PRESENT LAW

No provision.

REASONS FOR CHANGE

This provision authorizes the Secretary of Labor to provide the operating instructions necessary to ensure proper implementation of the changes proposed. Given the immediate nature of the transfers, the generally short-term nature of uses for transferred amounts, and likely State desire to begin using these funds as soon as possible to support benefit needs, it is anticipated that operating instructions will be provided by the U.S. Department of Labor as appropriate.

EXPLANATION OF PROVISION

The Secretary of Labor may prescribe any operating instructions or regulations necessary to carry out this section and amendments made by it.

TITLE V—HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED

A. Health Care Assistance for the Unemployed

PRESENT LAW

Title XX of the Social Security Act, referred to as the Social Services Block Grant (SSBG), provides flexible block grant funds to States to assist them in delivering a wide range of social services to needy children and adults. A service may be funded in its entirety, or it can be supplemented with other funding sources. State and local agencies may provide the services or purchase them from qualified agencies, organizations, or individuals. States are required to report annually on their expenditures of SSBG funds. In fiscal year 2001, $1.725 billion was appropriated for the SSBG program and was allotted to the States and Territories (Puerto Rico, Guam, the Virgin Islands, American Samoa, and the Northern Marianas). Allotments to States are by a formula based on population.

REASONS FOR CHANGE

The provision provides States additional funds to address the health care needs of unemployed workers and their families. Under this provision, which operates under an existing block grant program within the Human Resources jurisdiction of the Committee, States would have the flexibility to use new Federal funds to assist uninsured individuals in their communities. For example, the funds would be able to be used to defray the cost of private health coverage or coverage under existing State and local health care programs for which unemployed workers and their dependents would not otherwise be eligible.

EXPLANATION OF PROVISION

Funding for the Social Services Block Grant program would be increased by $3 billion in fiscal year 2002. The increased funding would be available to States only to assist in providing health care coverage for unemployed workers and their families who do not have other Federal health care coverage. Funds are to supplement (not supplant) any other Federal, State, or local funds used for health care coverage.

III. VOTES OF THE COMMITTEE

In compliance with clause 3(b) of rule XIII of the Rules of the House of Representatives, the following statements are made concerning the votes of the Committee on Ways and Means in its consideration of the bill, H.R. 3090.

MOTION TO REPORT THE BILL

The bill, H.R. 3090, as amended, was ordered favorably reported by a rollcall vote of 23 yeas to 14 nays (with a quorum being present). The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Thomas	X			Mr. Rangel		X	
Mr. Crane	X			Mr. Stark		X	
Mr. Shaw				Mr. Matsui		X	
Mrs. Johnson	X			Mr. Coyne		X	
Mr. Houghton	X			Mr. Levin		X	
Mr. Herger	X			Mr. Cardin		X	
Mr. McCrery	X			Mr. McDermott		X	
Mr. Camp	X			Mr. Kleczka		X	
Mr. Ramstad	X			Mr. Lewis (GA)		X	
Mr. Nussle	X			Mr. Neal		X	
Mr. Johnson	X			Mr. McNulty			
Ms. Dunn	X			Mr. Jefferson			
Mr. Collins	X			Mr. Tanner		X	
Mr. Portman	X			Mr. Becerra		X	
Mr. English	X			Mrs. Thurman		X	
Mr. Watkins	X			Mr. Doggett		X	
Mr. Hayworth	X			Mr. Pomeroy			
Mr. Weller	X						
Mr. Hulshof	X						
Mr. McInnis	X						
Mr. Lewis (KY)	X						
Mr. Foley	X						
Mr. Brady	X						
Mr. Ryan	X						

VOTES ON AMENDMENTS

A rollcall vote was conducted on the following amendment to the Chairman's amendment in the nature of a substitute.

An amendment by Mr. Stark, which would create a Federal subsidy equal to 75 percent of COBRA premiums for up to 12 months, and would not change the underlying eligibility for COBRA coverage, was defeated by a rollcall vote of 16 yeas to 25 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Thomas		X		Mr. Rangel	X		
Mr. Crane		X		Mr. Stark	X		

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Shaw		X		Mr. Matsui	X		
Mrs. Johnson		X		Mr. Coyne	X		
Mr. Houghton		X		Mr. Levin	X		
Mr. Herger		X		Mr. Cardin	X		
Mr. McCrery		X		Mr. McDermott	X		
Mr. Camp		X		Mr. Kleczka	X		
Mr. Ramstad		X		Mr. Lewis (GA)	X		
Mr. Nussle		X		Mr. Neal	X		
Mr. Johnson		X		Mr. McNulty	X		
Ms. Dunn	X			Mr. Jefferson	X		
Mr. Collins		X		Mr. Tanner		X	
Mr. Portman		X		Mr. Becerra	X		
Mr. English		X		Mrs. Thurman	X		
Mr. Watkins		X		Mr. Doggett	X		
Mr. Hayworth		X		Mr. Pomeroy		X	
Mr. Weller		X					
Mr. Hulshof		X					
Mr. McInnis		X					
Mr. Lewis (KY)		X					
Mr. Foley		X					
Mr. Brady		X					
Mr. Ryan		X					

An amendment by Messrs. Cardin and McDermott, that would add a new section to provide temporary unemployment compensation, was defeated by a rollcall vote of 18 yeas to 22 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Thomas		X		Mr. Rangel	X		
Mr. Crane		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Matsui	X		
Mrs. Johnson		X		Mr. Coyne	X		
Mr. Houghton	X			Mr. Levin	X		
Mr. Herger		X		Mr. Cardin	X		
Mr. McCrery		X		Mr. McDermott	X		
Mr. Camp		X		Mr. Kleczka		X	
Mr. Ramstad		X		Mr. Lewis (GA)	X		
Mr. Nussle		X		Mr. Neal			
Mr. Johnson		X		Mr. McNulty	X		
Ms. Dunn		X		Mr. Jefferson	X		
Mr. Collins		X		Mr. Tanner	X		
Mr. Portman		X		Mr. Becerra	X		
Mr. English	X			Mrs. Thurman	X		
Mr. Watkins		X		Mr. Doggett	X		
Mr. Hayworth		X		Mr. Pomeroy	X		
Mr. Weller		X					
Mr. Hulshof		X					
Mr. McInnis		X					
Mr. Lewis (KY)		X					
Mr. Foley		X					
Mr. Brady		X					
Mr. Ryan		X					

An amendment by Mr. Kleczka, which would eliminate the refundable credit for corporate AMT liabilities, was defeated by a rollcall vote of 13 yeas to 23 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Thomas		X		Mr. Rangel	X		
Mr. Crane		X		Mr. Stark	X		
Mr. Shaw				Mr. Matsui	X		
Mrs. Johnson		X		Mr. Coyne	X		
Mr. Houghton		X		Mr. Levin	X		

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Herger		X		Mr. Cardin			
Mr. McCrery		X		Mr. McDermott	X		
Mr. Camp		X		Mr. Kleczka	X		
Mr. Ramstad		X		Mr. Lewis (GA)	X		
Mr. Nussle		X		Mr. Neal	X		
Mr. Johnson		X		Mr. McNulty			
Ms. Dunn		X		Mr. Jefferson			
Mr. Collins		X		Mr. Tanner			
Mr. Portman		X		Mr. Becerra	X		
Mr. English		X		Mrs. Thurman	X		
Mr. Watkins		X		Mr. Doggett	X		
Mr. Hayworth		X		Mr. Pomeroy	X		
Mr. Weller		X					
Mr. Hulshof		X					
Mr. McInnis		X					
Mr. Lewis (KY)		X					
Mr. Foley		X					
Mr. Brady		X					
Mr. Ryan		X					

IV. BUDGET EFFECTS OF THE BILL

A. Committee Estimate of Budgetary Effects

In compliance with clause 3(d)(2) of the rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effects on the budget of the revenue provisions of the bill, H.R. 3090 as reported.

The bill is estimated to have the following effects on budget receipts for fiscal years 2002–2006:

ESTIMATED BUDGET EFFECTS OF THE REVENUE PROVISIONS CONTAINED IN H.R. 3090, THE ''ECONOMIC SECURITY AND RECOVERY ACT OF 2001,'' AS REPORTED BY THE COMMITTEE ON WAYS AND MEANS

[Fiscal years 2002–2006, in millions of dollars]

Provision	Effective	2002	2003	2004	2005	2006	2002–06
Cost Recovery Provisions							
1. 30% expensing of the value of capital assets with MACRS lives of 20 years or less and purchased software (sunset after 36 months) [1]	ppiso/a 9/11/01	−39,301	−36,125	−30,295	−6,904	22,299	−76,518
2. Increase in section 179 expensing to $35,000, and increase beginning point for phaseout to $325,000 for 24 months	tyba 12/31/01	−852	−1,406	−142	682	466	−1,251
3. 15-year life leasehold improvements [2]	lipiso/a 9/11/01	−78	−202	−369	−533	−684	−1,865
Total of Cost Recovery Provisions		−40,231	−37,733	−30,806	7,053	22,081	−79,634
Net Operating Loss Provision—5-Year Carryback of Net Operating Losses and Waive the AMT 90% Limitation on the Allowance of Losses (sunset after 36 months)	NOLs gi tyeo/a 9/11/01	−4,704	−3,528	−1,910	3,418	3,026	−3,699
Alternative Minimum Tax Provisions–Repeal the corporate AMT and fully refund AMT credits [3]	tyba 12/31/00	−25,397	822	1,209	736	189	−22,441
Deferral of Multinational Business Income Provision—Permanently extend exceptions under subpart F for active financing income	tyba 12/31/01	−260	−1,252	−1,441	−1,659	−1,911	−6,523
Provisions Affecting Individual Taxpayers							
1. Supplemental Rebate—Provide a rebate ($300 individual, $600 married filing jointly, and $500 head-of-household) for individuals who filed a tax return in 2000 other than dependents and nonresident aliens; rebate amount reduced by amount of rebate individual received under H.R. 1836 [4]	DOE	−13,733					−13,733
2. Accelerate the 25% individual income tax rate scheduled to go into effect in 2006 to 2002	tyba 12/31/01	−12,816	−18,862	−12,196	−7,685	−2,106	−53,665
3. Increase AMT exemption by $1,600 non-joint/$3,200 joint for 2002 and 2003, and $850 non-joint/$1,700 joint for 2004	tyba 12/31/01	−717	−2,063	−2,315	−1,250		−6,345
4. Increase deduction of capital losses of individuals against ordinary income from $3,000 to $4,000 for taxable year 2001 only and $5,000 for taxable year 2002 only	tyba 12/31/01	−840	−1,224	83	54	25	−1,903
5. Simplify individual capital gains—repeal mark-to-market and the 5-year holding period and allow adjusted net capital gains to qualify for the 18%/8% capital gains rates	soeo/a 10/12/01	−535	1,451	−1,033	−2,420	−2,385	−4,922
6. Expand the exemption from the early withdrawal tax for health insurance expenses for unemployed individuals	(5)	−13	−59	−33	1	1	−103
Total of Provisions Affecting Individual Taxpayers		−28,654	−20,757	−15,494	−11,300	−4,465	−80,671

ESTIMATED BUDGET EFFECTS OF THE REVENUE PROVISIONS CONTAINED IN H.R. 3090, THE ''ECONOMIC SECURITY AND RECOVERY ACT OF 2001,'' AS REPORTED BY THE COMMITTEE ON WAYS AND MEANS—Continued

[Fiscal years 2002–2006, in millions of dollars]

Provision	Effective	2002	2003	2004	2005	2006	2002–06
Extension of Expiring Provisions and Technical Amendments							
1. Two-year extension of provisions expiring in 2001:							
a. Treatment of nonrefundable personal credits under the individual alternative minimum tax [6]	tyba 12/31/01	−123	−664	−695	.....	.....	−1,482
b. Work opportunity tax credit	wpoifibwa 12/31/01	−92	−246	−247	−130	−51	−766
c. Welfare-to-work tax credit	wpoifibwa 12/31/01	−27	−79	−90	−54	−23	−272
d. Tax credit for electricity production from wind, closed-loop biomass, and poultry litter—facilities placed in service date	ppisa 12/31/01	−9	−26	−33	−34	−34	−136
e. Suspension of 100 percent-of-net-income limitation on percentage depletion for oil and gas from marginal wells	tyba 12/31/01	−27	−41	−14	.....	.....	−82
f. Qualified zone academy bonds	tyba 12/31/01	([7])	−2	−7	−14	−20	−43
g. Temporary increase in limit on cover over of rum excise tax revenues (from $10.50 to $13.25 per proof gallon) to Puerto Rico and the Virgin Islands [8]	DOE	−65	−61	−14	.....	.....	−140
h. Suspension of requirement that terminals selling diesel fuel and kerosene must sell both dyed and undyed fuel	DOE			Negligible Revenue Effect			
i. Deductions for clean-fuel vehicles and refueling property	ppisa 12/31/01 [9]	−9	−19	−18	−13	2	−57
j. Tax credit for electric vehicles	ppisa 12/31/01 [10]	−25	−43	−41	−34	−20	−163
k. Tax on failure to comply with mental health parity requirements applicable to group health plans	pybo/a 1/1/02			Negligible Revenue Effect			
2. One-year extension of provision expiring in 2002-Archer medical savings accounts (''MSAs'')	DOE	.....	([7])	−2	−2	−2	−7
3. Technical Amendments:							
a. Limit use of non-accrual experience method of accounting to amounts to be received for the performance of qualified professional services	tyea DOE	14	62	33	29	16	154
b. Reverse the Supreme Court's decision in Gitlitz v. Commissioner (relating to subchapter S corporations)	da 10/11/01	58	85	89	93	97	423
Total of Extension of Expiring Provisions and Technical Amendments	.....	−305	−1,034	−1,039	−159	−35	−2,571
Net total	.....	−99,551	−63,482	−49,481	−1,911	−18,885	−195,539

[1] A binding contract placed-in-service extension would apply in certain cases.
[2] Provision is not eligible for the 30% expensing provision.
[3] Includes outlay effect of $16,068 million in fiscal year 2002.
[4] Includes outlay effect of $13,733 million in fiscal year 2002.
[5] Effective for distributions made after the date of enactment to individuals who receive unemployment compensation for four consecutive weeks during the period from September 11, 2001, to December 31, 2002.

[6] The ''Economic Growth and Tax Relief Reconciliation Act of 2001'' provides that the child tax credit and adoption tax credit are allowed for purposes of the alternative minimum tax for 2002 through 2010.

[7] Loss of less than $500,000.

[8] Estimate provided by the Congressional Budget Office.

[9] The deduction phases down for vehicles placed in service after 12/31/03. The deductible amount is reduced by 25 percent in 2004, 50 percent in 2005, and 75 percent in 2006. No expensing is available after 2006.

[10] The credit phases down for vehicles placed in service after 12/31/03. The deductible amount is reduced by 25 percent in 2004, 50 percent in 2005, and 75 percent in 2006. No credit is available after 2006.

Legend for ''Effective'' column: da=discharges after; DOE=date of enactment; gi-generated in; lipiso/a=leasehold improvements placed in service on or after; NOLs=net operating losses; ppisa=property placed in service after; ppiso=property placed in service on or after; pybo/a=plan years beginning on or after; soeo/a=sales or exchanges on or after; tyba=taxable years beginning after; tyeo/a=taxable years ending after; tyeo/a=taxable years ending on or after; wpoifibwa=wages paid or incurred for individuals beginning work after.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

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 new or increased budget authority (as detailed in the statement by the Congressional Budget Office ("CBO"); see Part IV.C., below). The Committee further states that the revenue reducing income tax provisions involve increased tax expenditures. (See amounts in table in Part IV.A., above.)

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, October 17, 2001.

Hon. William "Bill" M. Thomas,
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. 3090, the Economic Security and Recovery Act of 2001.

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

Sincerely,

Dan L. Crippen,
Director.

Enclosure.

H.R. 3090—Economic Security and Recovery Act of 2001

Summary: H.R. 3090 would reduce tax receipts from corporations by increasing and extending certain deductions and exemptions and by repealing the alternative minimum tax. It also would provide a tax rebate to certain individual tax filers, accelerate the reduction of the prior-law 28 percent individual income tax rate of 25 percent in calendar years 2002 and thereafter, and reduce the rate at which capital gains are taxed for individuals. In addition, the bill would extend numerous tax credits and make certain other changes.

The Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) estimate that H.R. 3090 would decrease governmental receipts by $69.7 billion in 2002, by $164.7 billion over the 2002–2006 period, and by $128.2 billion over the 2002–2011 period. In addition, the bill would increase direct spending by $31.5 billion in 2002 and $2.7 billion in 203. In total, H.R. 3090 would reduce projected total surpluses by an estimated $162 billion over the 2002–2011 period. Because the bill would affect receipts and direct spending, pay-as-you-go procedures would apply.

The review of H.R. 3090 by JCT and CBO identified no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA). CBO reviewed four sections of the bill (sections 103,

310, 402, and 501), two of which would provide benefits to state governments: one by accelerating transfers of funds to state accounts for unemployment compensation benefits, and another by providing grants to states for health insurance assistance to unemployed individuals.

JCT has determined that the provisions that limit use of the nonaccrual experience method of accounting and that alter the treatment of discharge of indebtedness of an S corporation contain private-sector mandates. CBO has determined that section 301 of the bill, which extends the provisions of the Mental Health Parity Act, contains a private-sector mandate. CBO and JCT estimate that the direct cost of the private-sector mandates in the bill would exceed the annual threshold established by UMRA ($113 million in 2001, adjusted for inflation) in each of the years that the mandates would be effective.

Major provisions

Title I, entitled Business Provisions, would:

- Allow taxpayers to deduct an additional 30 percent of the value of certain qualifying capital assets and software in the first year if such property is placed in service before January 1, 2005;
- Increase the maximum dollar amount that may be deducted on qualifying property in lieu of depreciation from $24,000 ($25,000 in taxable years beginning after 2003) to $35,000 for property placed in service after December 31, 2001, and before January 1, 2004, and increase the beginning point at which such treatment is phased out to $325,000 before January 1, 2004;
- Allow taxpayers to depreciate certain improvements to leasehold property over 15 years;
- Extend to five years the period in which taxpayers may carry back net operating losses in taxable years arising on or after September 11, 2001, and ending before September 11, 2004;
- Repeal the corporate Alternative Minimum Tax (AMT) and make the AMT credit refundable; and
- Extend permanently the deferral of certain active financing income of multinational business.

Title II, entitled Individual Provisions, would:

- Accelerate the reduction of the prior-law 28 percent individual income tax rate to 25 percent in calendar year 2002 and thereafter;
- Increase the AMT exemption amount for individuals for taxable years beginning after December 31, 2001, and before January 1, 2005;
- Increase the deduction of capital losses of individuals against ordinary income from $3,000 to $4,000 for taxable year 2001, and to $5,000 for taxable year 2002;
- Reduce the tax rates on the adjusted net capital gain of an individual from 20 percent and 10 percent to 18 percent and 8 percent, respectively, and repeal the special rules for certain gain from property held more than five years; and
- Expand the exception of the tax on early withdrawal of IRA distributions to distribution used for health insurance by

unemployed individuals if those distributions were made by individuals between September 11, 2001, and December 31, 2002.

Title III, entitled Extensions of Certain Expiring Provisions, would:

- Allow an individual to offset all regular tax liability and AMT liability by personal nonrefundable credits in 2002 and 2003;
- Extend several tax credits for two years, including the work opportunity tax credit and the welfare-to-work tax credit;
- Allow new contributions to be made to Archer medical savings accounts through December 31, 2003, for those individuals who would no longer be able to contribute under current law;
- Extend the Mental Health Parity Act of 1996, which expired September 30, 2001, for an additional 2 years;
- Limit the use of the experience method of accounting; and
- Provide that income from the discharge of indebtedness of an S corporation not be taken into account as an item of income by any shareholder.

Title IV, entitled Supplemental Rebate; Other Provisions, would:

- Provide an additional rebate to those taxpayers who filed income tax returns for 2000 if they were eligible for rebates under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and did not receive the maximum rebate amount under the act; and
- Accelerate transfers from the federal unemployment accounts to the state accounts in the unemployment trust fund.

Title V, entitled Health Care Assistance for the Unemployed, would increase by $3 billion Social Services Block Grants to states for health care assistance for the unemployed.

Estimated cost to the Federal Government: The estimated budgetary impact of H.R. 3090 is shown in the following table. Most of the budgetary effects of the legislation are reductions in revenues. However, enacting the bill also would increase outlays by making the AMT credit refundable and by providing additional rebates to some taxpayers who were eligible for rebates under EGTRRA. Enacting H.R. 3090 also would increase outlays by accelerating transfers from the federal unemployment accounts to the state accounts in the unemployment trust fund. In addition, outlays would result from new grants to states for health insurance coverage for the unemployed. The spending effects of this legislation would fall within budget functions 500 (education, training, employment, and social services), 600 (income security), and 800 (general government).

Basis of estimate

Revenues

All the estimates for the revenue provisions, with the exception of the provision relating to unemployment trust fund revenues (detailed in the direct-spending section) and the provision relating to the extension of the Mental Health Parity Act of 1996 (detailed in the discussion of the private-sector impact), were provided by the JCT.

Of the provisions estimated by the JCT, four provisions would comprise the majority of the changes in revenues if H.R. 3090 were

enacted. The provisions that allow taxpayers to deduct an additional 30 percent of the value of certain assets, repeal the alternative minimum tax, extend permanently the deferral of certain active financing income of multinational businesses, and accelerate the reduction of the prior-law 28 percent individual income tax rate to 25 percent in calendar year 2002 would, if enacted, reduce revenues by an estimated $61.7 billion in 2002, $143.1 billion over the 2002–2006 period, and $100.9 billion over the 2002–2011 period.

Direct spending

Allow Corporations to Treat Alternative Minimum Tax Credits as Refundable. Under current law, if a corporation is subject to the AMT in any year, the amount of the AMT is allowed as a credit against income in any subsequent taxable year if the regular tax liability exceeds a certain amount. Under H.R. 3090, if the AMT credit exceeded the taxpayer's 2001 tax liability, the taxpayer would receive the excess as a refund. CBO considers that excess to be an outlay. CBO expects that all refunds of the credit—totaling $16.1 billion—would be made in 2002, and that there would be no future outlays for this purpose as the AMT would be repealed under the bill.

ESTIMATED BUDGETARY IMPACT OF H.R. 3090

	By fiscal year, in millions of dollars—				
	2002	2003	2004	2005	2006
CHANGES IN REVENUES					
Title I: Business Provisions	−54,981	−42,502	−33,822	9,957	25,296
Title II: Individual Provisions	−14,204	−18,694	−13,179	−10,050	−4,465
Title III: Extensions of Certain Expiring Provisions	−490	−2,295	−2,490	−1,818	−1,946
Title IV: Supplemental Rebate; Other Provisions	−0	100	300	300	300
Total Changes in Revenues	−69,675	−63,391	−49,191	−1,611	19,185
On-Budget	−69,670	−63,383	−49,188	−1,611	19,185
Off-Budget	−5	−8	−3	0	0
CHANGES IN DIRECT SPENDING					
Outlays for Refundable AMT Credit	16,068	0	0	0	0
Outlays for Supplemental Rebate	13,733	0	0	0	0
Accelerated Transfer to State Unemployment Trust Fund [1]	700	700	0	0	0
Increase in Social Services Block Grant	1,000	2,000	0	0	0
Total Changes in Direct Spending Outlays	31,501	2,700	0	0	0
Net Increase or Decrease (-) in the Budget Surplus	−101,176	−66,091	−49,191	1,611	19,185

[1] Under more realistic assumptions about likely unemployment in the near term, CBO would expect the increase in outlays to be greater in the short term—totaling about $4.5 billion in fiscal years 2002 and 2003. However, this increase in spending would be completely offset by revenue increases and by reduced spending in the following seven fiscal years.

Sources: Joint Committee on Taxation and Congressional Budget Office.

Supplemental Rebate. The bill would provide an additional rebate to those taxpayers who filed a tax return for 2000 and were eligible for payment under the advance refund mechanism in EGTRRA but who did not receive the maximum amount ($300 for individual taxpayers or married taxpayers filing separately, $500 for taxpayers filing as heads of households, and $600 for married taxpayers filing jointly). Under normal budgetary procedures, the amount of a rebate or refundable tax credit that exceeds an individual's tax liabilities is considered a form of spending, rather than

an offset to revenues. This supplemental rebate falls in spending category because, under current law, taxpayers have received (in 2001) or will receive (in 2002) credits allowed under EGTTRA at least up to the amounts of their 2001 tax liabilities. Thus, the supplemental rebates represent amounts in excess of individuals' tax liabilities for 2001 and should be classified as outlays.

JCT estimates that the additional refunds will total about $13.7 billion. CBO expects that all outlays would be made in fiscal year 2002.

Transfers from Federal Unemployment Accounts. Section 402 of the bill would accelerate transfers from the federal unemployment accounts to the state accounts in the unemployment trust fund. CBO estimates that roughly $40 billion of these transfers could be anticipated over the 2002–2011 period under provisions of current law. The bill would provide for the immediate transfer of $9.3 billion from federal accounts to the state accounts in the unemployment trust fund, amounts that the states otherwise would receive during the 2003–2005 period. States would be allowed to spend those funds on unemployment compensation or on administrative costs associated with unemployment and employment services.

CBO expects that states would spend a portion of these funds in fiscal years 2002 and 2003. Under the economic assumptions underlying the budget resolution, the additional outlays are estimated to total $1.4 billion over the next two years. If unemployment rates were to approach 6.0 percent in 2002, CBO estimates the additional spending would be somewhat higher—about $4.5 billion—during the 2002–2003 period. However, over the longer run, this additional spending would be completely offset by increases in state revenues and by some reductions in spending. The offsets in future years occur because the reserve ratios in the state trust funds (the amount of funds kept on hand to pay future benefits) are assumed to remain in balance. Therefore, increased spending in the short term would be offset by decreased spending or increased revenues in the longer term. Thus, speeding up the transfer would have no net cost over the 2002–2011 period.

Health Care Coverage for the Unemployed. Section 501 would increase the amount of the Social Services Block Grant by $3 billion in 2002 to provide health care coverage for the unemployed. The money would be allocated to states based on their population. States could use the money to provide health coverage for individuals (or family members of such individuals) who qualify for unemployment benefits in calendar year 2001 or later, and are not otherwise eligible for federal health coverage.

CBO expects that it would take several months for states to establish eligibility criteria and delivery mechanisms for the new services. CBO projects that $1 billion would be spent in 2002 and $2 billion in 2003.

Pay-as-you-go-considerations: The net changes in outlays and governmental receipts that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects in the current year and the succeeding four years are counted.

	By fiscal year, in millions of dollars—									
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Changes in receipts	−69,665	−63,381	−49,191	−1,611	19,185	15,841	11,762	7,160	2,804	−1,043
Changes in outlays	31,501	2,700	0	0	0	0	0	0	0	0

Impact on State, local, and tribal governments: H.R. 3090 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA). Two of the provisions reviewed by CBO would provide benefits to state governments.

Section 402 of the bill would accelerate transfers from federal accounts in the unemployment trust fund to state unemployment compensation accounts. States would be able to use these additional funds, estimated to total $9.3 billion, for the payment of regular unemployment benefits as established in state laws or for the payment of new benefits established at the option of the state through March 11, 2003.

Section 501 of the bill would provide $3 billion to states through the Social Services Block Grant program to help unemployed individuals acquire health care coverage. The funds could not be used to supplant any other federal, state, or local funds that are used for health care coverage. In order to be eligible for assistance, an individual could not be eligible for any other federal health coverage.

Impact on the private sector: CBO and JCT estimate that the cost of the private-sector mandates in the bill would exceed the annual threshold established by UMRA ($113 million in 2001, adjusted for inflation) in each of the years that the mandates would be effective.

Mental Health Parity. Section 310 would extend the provisions of the Mental Health Parity Act of 1996, which expired on September 30, 2001, for an additional two years. That act prohibited group health plans that provide both medical and surgical benefits and mental health benefits from imposing aggregate lifetime limits or annual limits for coverage of mental health benefits that are different from those used for medical and surgical benefits. CBO estimates that the direct cost of the private-sector mandate in section 310 would be $270 million in fiscal year 2002 and $400 million in fiscal year 2003.

CBO estimates that the provision, if enacted, would increase premiums for group health insurance by an average of 0.1 percent, before accounting for the responses of health plans, employers, and workers to the higher premiums under the bill. CBO assumes that 60 percent of the potential impact of the mandate would be offset by behavioral responses, such as reductions in the number of employers offering insurance to their employees and in the number of employees enrolling in employer-sponsored insurance, changes in the types of heath plans that are offered, and reductions in the scope or generosity of health insurance benefits. The remaining 40 percent of the potential increase in costs, or about 0.04 percent of group health insurance premiums, would occur in the form of increased outlays for health insurance. Those costs would be passed through to employees of private firms, reducing both their taxable compensation and other fringe benefits. CBO estimates that the resulting reduction in taxable income would be $76 million in calendar year 2002 and $85 million in calendar year 2003.

Those reductions in workers' taxable compensation would lead to lower federal tax revenues. CBO estimates that, as a result of the mental health parity provisions, federal tax revenues would fall by $20 million in fiscal year 2002, by $30 million in 2003, and by $10 million in 2004 if H.R. 3090 were enacted. Social Security payroll taxes, which are off-budget, would account for about 30 percent of the total.

Other Mandates. Section 341 of the bill would provide that income from the discharge of indebtedness of an S corporation that is excluded from the S corporation's income is not taken into account as an item of income by any shareholder and thus does not increase the basis of any shareholder's stock in the corporation.

Under Section 342, the experience method of accounting would be available only for amounts to be received for the performance of qualified services and for services provided by certain small businesses.

JCT estimates that those private-sector mandates in the bill would exceed the annual threshold established by UMRA ($113 million in 2001, adjusted for inflation) in each of the years that the mandates would be effective.

Estimate prepared by: Federal Revenues: Erin Whitaker and Alexis Ahlstrom. Transfer to State Unemployment Trust Funds: Christi Hawley Sadoti. Health Care Coverage for the Unemployed: Sheila Dacey. Impact on State, Local, and Tribal Governments: Leo Lex. Impact on the Private Sector: Jen Bullard Bowman.

Estimate approved by: G. Thomas Woodward, Assistant Director for Tax Analysis; Robert A. Sunshine, Assistant Director for Budget Analysis.

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

A. Committee Oversight Findings and Recommendations

With respect to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives (relating to oversight findings), the Committee advises that it was a result of the Committee's oversight review of any conditions or circumstances that may indicate the necessity or desirability of enacting new or additional legislation within its jurisdiction that the Committee determined that there is a need for tax legislation and legislation relating to unemployment to aid in providing economic security and recovery in light of the events of September 11, 2001, and the current state of the U.S. economy.

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 performance goals and objectives of that part of the tax provisions in this legislation that authorize funding (i.e., providing supplemental rebates and repeal of the corporate alternative minimum tax) are to stimulate the economy and increase consumer confidence by providing additional cash to taxpayers. In addition, the provisions of the bill relating to transferring Federal unemployment and health funds to the States will assist unemployed workers and their dependents.

C. Constitutional Authority Statement

With respect to clause 3(d)(1) of the rule XIII of the Rules of the House of Representatives (relating to Constitutional Authority), the Committee states that the Committee's action in reporting this bill is derived from Article I of the Constitution, Section 8 ("The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises * * * "), and from the 16th Amendment to the Constitution.

D. Information Relating to Unfunded Mandates

This information is provided in accordance with section 423 of the Unfunded Mandates Act of 1995 (P.L. 104–4).

The Committee has determined that the following provisions of the bill contain Federal private sector mandates: (1) limit use of the non-accrual method of accounting; and (2) discharge of indebtedness of an S corporation. The costs required to comply with each of these private sector mandates generally are no greater than the estimated budget effects of the provision as reflected in Part IV.A., above. These provisions provide revenue offsets for the economic stimulus provisions of the bill and also improve the operation of the Federal income tax system by resulting in a more accurate measurement of income in those situations affected by the provision.

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

E. 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 provisions of the bill, and states that the provisions of the bill do not involve any Federal income tax rate increases within the meaning of the rule.

F. Tax Complexity Analysis

The following tax complexity analysis is provided pursuant to section 4022(b) of the Internal Revenue Service Reform and Restructuring Act of 1998, which requires the staff of the Joint Committee on Taxation (in consultation with the Internal Revenue Service ("IRS") and the Treasury Department) to provide a complexity analysis of tax legislation reported by the House Committee on Ways and Means, the Senate Committee on Finance, or a Conference Report containing tax provisions. The complexity analysis is required to report on the complexity and administrative issues raised by provisions that directly or indirectly amend the Internal Revenue Code and that have widespread applicability to individuals or small businesses. For each such provision identified by the staff of the Joint Committee on Taxation, a summary description of the provision is provided 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 the Treasury Department regarding each of the provisions included in the complexity analysis, including a discussion of the likely effect on IRS forms and any expected impact on the IRS.

1. Special Depreciation Allowance for Certain Property (sec. 101 of the bill)

Summary description of provision

The bill allows an additional first-year depreciation deduction equal to 30 percent of the adjusted basis of certain qualified property that is placed in service before January 1, 2005. The additional depreciation deduction is allowed for both regular tax and alternative minimum tax purposes for the taxable year in which the property is placed in service. The basis of the property and the depreciation allowances in the year of purchase and later years is appropriately adjusted to reflect the additional first-year depreciation deduction. A taxpayer can elect not to claim the additional first-year depreciation for qualified property.

In general, property will qualify for the additional first-year depreciation deduction if the property is (1) property to which the modified accelerated cost recovery system ("MACRS") applies with a recovery period of 20 years or less except for leasehold improvements, (2) water utility property as defined in section 168(e)(5), or (3) computer software other than computer software covered by section 197. In order to be qualified property, the original use of the property must commence with the taxpayer on or after September 11, 2001. A special rule precludes the additional first-year depreciation deduction for property that is required to be depreciated under the alternative depreciation system of MACRS. In addition, generally qualified property is required to be acquired by the taxpayer after September 10, 2001 and before September 11, 2004.

Number of affected taxpayers

It is estimated that more than 10 percent of small businesses will be affected by the provision.

Discussion

It is not anticipated that small businesses will have to keep additional records due to this provision, nor will additional regulatory guidance be necessary to implement this provision. It is not anticipated that the provision will result in an increase in disputes between small businesses and the IRS. However, small businesses will have to perform additional analysis to determine whether property qualifies for the provision. In addition, for qualified property, small businesses will be required to perform additional calculations to determine the proper amount of allowable depreciation. Complexity may also be increased because the provision is temporary. For example, different tax treatment will apply for identical equipment based on the acquisition and placed in service date. Further, the Secretary of the Treasury is expected to have to make appropriate revisions to the applicable depreciation tax forms.

2. Accelerate the 25-Percent Rate Bracket to 2002 (sec. 201(a) of the bill)

Summary description of provision

The Economic Growth and Tax Relief Reconciliation Act of 2001 reduced the prior-law 28-percent individual regular income tax rate to 25 percent. This rate reduction is phased-in over six years. The rate is 27 percent for taxable years beginning in calendar years 2001–2003, 26 percent for taxable years beginning in calendar years 2004–2005, and 25 percent for taxable years beginning in calendar years 2006 and thereafter. The bill accelerates this reduction. Therefore, the 25-percent rate is effective for taxable years beginning in calendar years 2002 and thereafter.

Number of affected taxpayers

It is estimated that the provision will affect approximately 37 million individual tax returns per year.

Discussion

It is not anticipated that individuals will need to keep additional records due to this provision. It should not result in an increase in disputes with the IRS, nor will regulatory guidance be necessary to implement this provision. In addition, the provision should not increase the tax preparation costs for most individuals.

3. Simplify Individual Capital Gains Rates (sec. 202 of the bill)

Summary description of provision

The provision repeals the special rules for certain gain from property held more than five years and repeals the mark to market election for certain property held on January 1, 2001. Thus, the present-law eight and 18 percent rates on adjusted net capital gains would apply to assets held more than one year.

Number and type of affected taxpayers

It is estimated that reducing the tax rates on capital gains will affect over 20 million taxpayers per year. It is estimated that, of this number, over ten million individual income tax returns have incomes of less than $75,000.

Discussion

It is not anticipated that individuals will need to keep additional records due to this provision, because the provision is only a rate change. Additional regulatory guidance should not be necessary to implement this provision. The provision should not increase the tax preparation cost of individuals using a tax preparation service, except possibly for the year 2001 when both the eight-percent and ten-percent rate schedules will be in effect for certain taxpayers. After 2001, the provision should result in simplification in computing the tax on capital gains (e.g. the tax form for computation of capital gains will be shortened and the calculation simplified). It is anticipated that eliminating the mark-to-market election will also reduce the record keeping and reporting burden on taxpayers. It is also anticipated that it will ease the administrative burden on the IRS.

4. Supplemental Rebate (sec. 401 of the bill)

Summary description of provision

The bill provides a supplemental rebate. Individuals who filed income tax returns for 2000 (regardless of whether they had any income tax liability or any payroll tax liability) are eligible for this supplemental rebate. The amount of the rebate is calculated in the following manner: taxpayers are eligible for the maximum rebate amount for their filing status ($300 single or married filing separately, $500 head of household, $600 joint filers) minus the amount (if any) of any previous rebate check issued.

Number of affected taxpayers

It is estimated that the provision will affect approximately 38 million individual tax returns per year.

Discussion

It is not anticipated that individuals will need to keep additional records due to this provision. In addition, the provision should not increase the tax preparation costs for most individuals. It should not result in an increase in disputes with the IRS, nor will regulatory guidance be necessary to implement this provision. It may, however, increase the number of questions that taxpayers ask the IRS, such as when taxpayers will receive their checks. This increased volume of questions could have an adverse impact on other elements of IRS' operations, such as the levels of taxpayer service. The IRS is expected to send notices to taxpayers who will be receiving supplemental rebates, which may reduce the number of questions from taxpayers.

The IRS will have a very short period of time in which to program its computers, test those programs, determine who should receive a supplemental rebate and in what amount, notify those taxpayers, and authorize the issuance of the supplemental rebates.[36] This may be difficult to do. In addition, doing these tasks may have unforeseen adverse consequences for other IRS responsibilities, such as the 2002 filing season.

DEPARTMENT OF THE TREASURY,
INTERAL REVENUE SERVICE,
Washington, DC, October 17, 2001.

MS. LINDY L. PAULL,
Chief of Staff, Joint Committee on Taxation,
Washington, DC

DEAR MS. PAULL: Enclosed are the combined comments of the Internal Revenue Service and the Treasury Department on the four provisions from the House Committee on Ways and Means markup of the "Economic Security and Recovery Act of 2001," that you identified for complexity analysis in your letter of October 12, 2001.

Our comments on provisions other than the supplemental rebate are based on the description of those provisions in JCX–69–01, Joint Committee on Taxation, Description of the Economic Security and Recovery Act of 2001, as introduced, October 11, 2001, and the

[36] The Financial Management Service of the Department of the Treasury, not the Internal Revenue Service, prints and mails the checks.

statutory language contained in H.R. 3090, as modified by the Amendment in the Nature of a Substitute Offered by Mr. Thomas. Our description and comments on the supplemental rebate provision are based solely on the description of that provision provided in the attachment to your letter of October 12.

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,

CHARLES O. ROSSOTTI.

Enclosure.

COMPLEXITY ANALYSIS OF PROVISIONS FROM THE "ECONOMIC SECURITY AND RECOVERY ACT OF 2001"

SPECIAL DEPRECIATION ALLOWANCE FOR CERTAIN PROPERTY

Provision: The proposal would allow an additional first-year depreciation deduction of 30 percent, for both regular and AMT property acquired after September 10, 2001 and before September 11, 2004, and placed in service before January 1, 2005. The basis of the property and depreciation in subsequent years would be appropriately adjusted to reflect the additional first-year depreciation. Taxpayers would be allowed to elect out of the additional first-year depreciation.

IRS and Treasury comments

• The special depreciation allowance would require changes to Form 4562 for 2001. One line would be added to Part I of the form. In addition, changes to the instructions for Form 2106 and 4562 would be necessary to explain the new rules. Taxpayers would be required to keep records of the amount of additional depreciation claimed on each asset in order to figure depreciation in later years.

SUPPLEMENTAL REBATE

Provision: A supplemental rebate would be available for individuals who filed income tax returns for 2000, even if they did not have any income tax liability, payroll tax liability, or wages for 2000. The amount of the rebate would be calculated in the following manner: taxpayers would be eligible for the maximum rebate amount for their filing status ($300 single or married filing separately, $500 head of household, $600 joint filers) minus the amount (if any) of any previous rebate check issued. Thus, if a single filer received $100 earlier this year as his or her rate reduction credit, he or she would receive an additional $200. Those who earlier received the full amounts for their filing status would not receive any supplemental rebate. Dependents and nonresident aliens would not be eligible for the supplemental rebates.

IRS and Treasury comments

• A mechanism for delivering the supplemental credit would have to be developed.

• Providing rebate checks to affected taxpayers before the end of 2001 may not be a viable delivery option.

• In order to compute, account for, control, and produce rebate checks, certain complex computer programs and systems must be

modified, tested, integrated with existing programs, and put into place, IRS would also need to modify the notice programs to reflect these new calculations and coordinate the issuance of checks with FMS.

• Revisions of this kind late in the calendar year always create extremely high risk of major errors in processing taxpayer returns. The problem is especially severe this year because significant technical and management resources were diverted from our development of programs for the 2002 filing season to accommodate the advance payments provided by the Economic Growth and Tax Relief Reconciliation Act of 2001, and the delayed due dates for certain taxpayers affected by the terrorist attacks of September 11, 2001. Currently, every available technical and management resource is operating at maximum capacity to ensure that programming for the 2002 filing season is completed timely. Attempting to implement programs to issue a "supplemental rebate" by December 31, 2001 would create serious risks of delay in the start of the 2002 filing season.

• Another approach would be to issue the supplemental rebate during the processing of an individual's 2001 tax return. This could be done by computing the additional rebate on the 2001 return and adjusting the 2001 balance due or refund to reflect the additional amount.

ACCELERATE THE 25-PERCENT RATE BRACKET TO 2002

Provision: The 25-percent rate (provided by the Economic Growth and Tax Relief Reconciliation Act of 2001) would be effective for taxable years beginning in calendar years 2002 and thereafter.

IRS and Treasury comments

• This tax rate change would be incorporated in the tax tables, tax rate schedules, withholding tables, and withholding rate schedules for 2002 during IRS' annual update of these items. Changes to the tax rates shown in the instructions for Forms 1040, 1040A, 1040EZ, and 1040NR, and on Forms 1040–ES and W–4V would be required for 2002. No new forms would be required. Programming changes to the tax computation process would be required to reflect the new rates.

SIMPLIFY INDIVIDUAL CAPITAL GAINS RATES

Provision: The proposal would reduce the 10 and 20 percent rates on adjusted net capital gain to 8 and 18 percent rates, respectively. (The special rules allowing reduced rates for property held for more than 5 years, and related election to recognize certain gain on property held on January 1, 2001 would be repealed because they are no longer necessary.) The reduced capital gain rates would apply, generally, to capital assets sold or exchanged on or after October 12, 2001.

IRS and Treasury comments

TAX FORMS

• Applying the reduced rates to gains after October 11, 2001 would require the following major changes to the 2001 Schedule D

(Form 1040) and the worksheets in its Instructions and the instructions for Forms 1040 and 1040A:

• In Part I of Schedule D, a new column with 5 lines for short-term gain or loss after October 11, 2001 would be added.

• In Part II, column (g) would be redesignated for gain or loss after October 11, 2001, and one entry space in that column would be removed.

• A new 8-line worksheet would be added to the Schedule D Instructions to determine 28 percent rate gain or loss (previously figured in column (g), Part II).

• In Part IV, 4 lines would be added to the computation of the amount taxed at 8 percent, and 8 lines would be added to figure the amount taxed at 18 percent and 20 percent. One line would be removed because its calculation would be done in the new worksheet for 28 percent rate gain or loss. The same changes (a net increase of 11 lines) would also be required for the new Schedule D Tax Worksheet in the Instructions for Schedule D.

• The two 15-line Capital Gain Tax Worksheets in the Instructions for Forms 1040 and 1040A could not be used and would have to be deleted. Most taxpayers whose only capital gains are capital gain distributions can now figure their tax on that worksheet instead of completing Schedule D. This change would require approximately 2 million taxpayers who file Form 1040A to instead file Form 1040 and complete Schedule D. Also, approximately 6 million Form 1040 filers would have to file Schedule D instead of using the worksheet. IRS could not allow taxpayers to use the worksheets because IRS would not have the information regarding gains and losses after October 11, 2001 necessary to math-verify the taxpayer's tax computation. IRS can only get this information by requiring the taxpayer to file Schedule D. IRS would also have to delete the checkbox from Form 1040 that indicates that the taxpayer had only capital gain distributions and used the Capital Gain Tax Worksheet instead of filing Schedule D.

• The October 12, 2001 effective date would also require conforming changes for the following 2001 forms: Schedule D–1 (Form 1040); Schedules D for Forms 1041, 1065, and 1120S; and Forms 2439, 4797, 6251, and 6781. In addition, the 2001 Schedules K–1 for Forms 1041, 1065, and 1120S would need to be revised to add lines for short-term, and section 1231 gain or loss after October 11, 2001. Finally, the 2001 Forms 1099–DIV and 1099–B should be revised to reflect the change. However, because they have already been printed and distributed, the IRS would have to issue an announcement explaining how the filers of those forms must report gain or loss after October 11, 2001 to the recipients on a substitute or separate statement. No new forms would be required.

• The added complexity of the 2001 Schedule D would lead to increased taxpayer error. During processing, these returns would have to be sent to Error Resolution for correction. This could cause additional delay in return processing and in the issuance of refunds. It also would increase IRS processing costs.

• Generally, the above changes apply only to the 2001 forms and instructions. The forms and instructions for 2002 and later years, including 2006, would be simpler than they would be absent this legislation. The four new lines in Part IV necessary to figure the amount taxed at 8 percent for 2001 (absent this legislation), as well

as the new 7-line Qualified 5-Year Gain Worksheet, would no longer be necessary. Also, IRS would not have to add similar additional lines and another worksheet in 2006 to accommodate the 18 percent tax rate on post-2000 qualified 5-year gain.

• Fiscal year 2000–2001 taxpayers with a taxable year ending after October 11, 2001 may also be affected. These taxpayers file 2000 tax forms, which are already in print. The IRS would have to issue an announcement similar to Announcement 97–109, 1997–45 I.R.B. 12, which was issued to reflect new reporting requirements mandated by the 1997 capital gains tax rate changes. The announcement would explain how taxpayers must complete their 2000 forms to reflect the reduced rates for net capital gain after October 11, 2001. The affected 2000 forms include Schedules D for Forms 1040 and 1041 and Schedules K–1 for Forms 1041, 1065, and 1120S.

PROGRAMMING AND PROCESSING

• The changes needed to the 2001 forms caused by the October 12, 2001 effective date would require extensive revision of computer programs and record layouts for processing those returns. Revisions of this kind late in the calendar year always pose extreme difficulties. The problem is especially severe this year because of the additional resources required to implement the Economic Growth and Tax Relief Reconciliation Act of 2001 (enacted in June 2001), conforming changes to that Act approved by the leadership of the tax writing committees in September 2001, and the delayed due dates for certain taxpayers affected by the terrorist acts on September 11, 2001.

• The IRS is currently working on these programming changes in preparation for the 2002 filing season. These changes are scheduled for completion by November 19, 2001. By mid-November 2001, all systems need to be frozen in order to allow for final end-to-end testing of IRS systems. The IRS also must work with independent vendors of tax preparation software to test their systems so that it can correctly receive electronically filed returns beginning shortly after January 1, 2002.

• If the October 12, 2001 effective date is retained, the IRS would be forced to complete testing of computer programs for processing during the 2002 filing season using existing law and would be unable to process 2001 returns reporting capital gains under the new law until later in the filing season, possibly not until March 2002. At a minimum, this means that taxpayers (including taxpayers who file electronically) who have capital gains and who are due refunds would not be able to receive their refunds until late in the filing season. In addition, since the over 28 million returns that include Schedule D would not be processed until late in the season during the peak filing period, processing of some other returns might be delayed. With delays for so many returns, the IRS would expect an increased number of taxpayer phone calls concerning, refunds, thereby reducing the opportunity for other taxpayers to get assistance.

VI. 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 italics, 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.

* * * * * * *

[Part VII. Environmental tax.]

PART I—TAX ON INDIVIDUALS

* * * * * * *

SEC. 1. TAX IMPOSED.

(a) * * *

* * * * * * *

(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) * * *

(B) [10] *8* 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, over

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

* * * * * * *

(C) [20] *18* percent of the adjusted net capital gain (or, if less, taxable income) in excess of the amount on which a tax is determined under subparagraph (B);

* * * * * * *

[(2) REDUCED CAPITAL GAIN RATES FOR QUALIFIED 5-YEAR GAIN.—

[(A) REDUCTION IN 10-PERCENT RATE.—In the case of any taxable year beginning after December 31, 2000, the rate under paragraph (1)(B) shall be 8 percent with respect to so much of the amount to which the 10-percent rate would otherwise apply as does not exceed qualified 5-year gain, and 10 percent with respect to the remainder of such amount.

[(B) REDUCTION IN 20-PERCENT RATE.—The rate under paragraph (1)(C) shall be 18 percent with respect to so much of the amount to which the 20-percent rate would otherwise apply as does not exceed the lesser of—

[(i) the excess of qualified 5-year gain over the amount of such gain taken into account under subparagraph (A) of this paragraph; or

[(ii) the amount of qualified 5-year gain (determined by taking into account only property the holding period for which begins after December 31, 2000), and 20 percent with respect to the remainder of such amount. For purposes of determining under the preceding sentence whether the holding period of property begins after December 31, 2000, the holding period of property acquired pursuant to the exercise of an option (or other right or obligation to acquire property) shall include the period such option (or other right or obligation) was held.]

[(3)] *(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).

[(4)] *(3)* ADJUSTED NET CAPITAL GAIN.—For purposes of this subsection, the term "adjusted net capital gain" means net capital gain reduced (but not below zero) by the sum of—

(A) unrecaptured section 1250 gain; and

(B) 28-percent rate gain.

[(5)] *(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

* * * * * * *

[(6)] *(5)* COLLECTIBLES GAIN AND LOSS.—For purposes of this subsection—

(A) * * *

* * * * * * *

[(7)] *(6)* UNRECAPTURED SECTION 1250 GAIN.—For purposes of this subsection—

(A) * * *

* * * * * * *

[(8)] *(7)* SECTION 1202 GAIN.—For purposes of this subsection, the term "section 1202 gain" means the excess of—

(A) * * *

* * * * * * *

[(9) QUALIFIED 5-YEAR GAIN.—For purposes of this subsection, the term "qualified 5-year gain" means the aggregate long-term capital gain from property held for more than 5 years. The determination under the preceding sentence shall be made without regard to collectibles gain, gain described in paragraph (7)(A)(i), and section 1202 gain.]

[(10)] *(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.

[(11)] *(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.

[(12)] *(10)* PASS-THRU ENTITY DEFINED.—For purposes of this subsection, the term "pass-thru entity" means—

(A) * * *

* * * * * * *

(i) RATE REDUCTIONS AFTER 2000.—

(1) * * *

(2) REDUCTIONS IN RATES AFTER JUNE 30, 2001.—In the case of taxable years beginning in a calendar year after 2000, the corresponding percentage specified for such calendar year in the following table shall be substituted for the otherwise applicable tax rate in the tables under subsections (a), (b), (c), (d), and (e).

In the case of taxable years beginning during calendar year:	The corresponding percentages shall be substituted for the following percentages:			
	28%	**31%**	**36%**	**39.6%**
2001	27.5%	30.5%	35.5%	39.1%
2002 and 2003	[27.0%] *25.0%*	30.0%	35.0%	38.6%
2004 and 2005	[26.0%] *25.0%*	29.0%	34.0%	37.6%
2006 and thereafter	25.0%	28.0%	33.0%	35.0%

* * * * * * *

PART II—TAX ON CORPORATIONS

* * * * * * *

SEC. 11. TAX IMPOSED.

(a) * * *

* * * * * * *

(d) FOREIGN CORPORATIONS.—In the case of a foreign corporation, [the taxes imposed by subsection (a) and section 55] *the tax imposed by subsection (a)* shall apply only as provided by section 882.

SEC. 12. CROSS REFERENCES RELATING TO TAX ON CORPORATIONS.

(1) * * *

* * * * * * *

[(7) For alternative minimum tax, see section 55.]

* * * * * * *

PART IV—CREDIT AGAINST TAX

* * * * * * *

Subpart A—Nonrefundable Personal Credits

* * * * * * *

SEC. 24. CHILD TAX CREDIT.

(a) * * *

* * * * * * *

(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) * * *

(B) the amount by which the [amount of credit allowed by this section] *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) * * *

* * * * * * *

SEC. 26. LIMITATION BASED ON TAX LIABILITY; DEFINITION OF TAX LIABILITY.

(a) LIMITATION BASED ON AMOUNT OF TAX.—

(1) * * *

(2) SPECIAL [RULE FOR 2000 AND 2001.—] *RULE FOR 2000, 2001, 2002, AND 2003*.—For purposes of any taxable year beginning [during 2000 or 2001,] *during 2000, 2001, 2002, or 2003,* the aggregate amount of credits allowed by this subpart for the taxable year shall not exceed the sum of—

(A) * * *

* * * * * * *

(b) REGULAR TAX LIABILITY.—For purposes of this part—

(1) * * *

(2) EXCEPTION FOR CERTAIN TAXES.—For purposes of paragraph (1), any tax imposed by any of the following provisions shall not be treated as tax imposed by this chapter:

(A) section 55 (relating to minimum tax),

[(B) section 59A (relating to environmental tax),]

[(C)] *(B)* subsection (m)(5)(B), (q), (t), or (v) of section 72 (relating to additional taxes on certain distributions),

[(D)] *(C)* section 143(m) (relating to recapture of proration of Federal subsidy from use of mortgage bonds and mortgage credit certificates),

[(E)] *(D)* section 530(d)(3) (relating to additional tax on certain distributions from education individual retirement accounts),

[(F)] *(E)* section 531 (relating to accumulated earnings tax),

[(G)] *(F)* section 541 (relating to personal holding company tax),

[(H)] *(G)* section 1351(d)(1) (relating to recoveries of foreign expropriation losses),

[(I)] *(H)* section 1374 (relating to tax on certain built-in gains of S corporations),

[(J)] *(I)* section 1375 (relating to tax imposed when passive investment income of corporation having subchapter C earnings and profits exceeds 25 percent of gross receipts),

[(K)] *(J)* subparagraph (A) of section 7518(g)(6) (relating to nonqualified withdrawals from capital construction funds taxed at highest marginal rate),

[(L)] *(K)* sections 871(a) and 881 (relating to certain income of nonresident aliens and foreign corporations),

[(M)] *(L)* section 860E(e) (relating to taxes with respect to certain residual interests),

[(N)] *(M)* section 884 (relating to branch profits tax),

[(O)] *(N)* sections 453(l)(3) and 453A(c) (relating to interest on certain deferred tax liabilities),

[(P)] *(O)* section 860K (relating to treatment of transfers of high-yield interests to disqualified holders), and,

[(Q)] *(P)* section 220(f)(4) (relating to additional tax on Archer MSA distributions not used for qualified medical expenses).

* * * * * * *

Subpart B—Other Credits

* * * * * * *

SEC. 29. CREDIT FOR PRODUCING FUEL FROM A NONCONVENTIONAL SOURCE.

(a) * * *

(b) LIMITATIONS AND ADJUSTMENTS.—

(1) * * *

* * * * * * *

[(6) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of—

[(A) the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and section 27, over

[(B) the tentative minimum tax for the taxable year.]

(6) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and section 27. In the case of a taxpayer other than a corporation, such excess shall be further reduced (but not below zero) by the tentative minimum tax for the taxable year.

* * * * * * *

SEC. 30. CREDIT FOR QUALIFIED ELECTRIC VEHICLES.

(a) * * *

(b) LIMITATIONS.—

(1) * * *

(2) PHASEOUT.—In the case of any qualified electric vehicle placed in service after December 31, [2001] *2003*, the credit otherwise allowable under subsection (a) (determined after the application of paragraph (1)) shall be reduced by—

(A) 25 percent in the case of property placed in service in calendar year [2002] *2004*,

(B) 50 percent in the case of property placed in service in calendar year [2003] *2005*, and

(C) 75 percent in the case of property placed in service in calendar year [2004] *2006*.

[(3) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of—

[(A) the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and sections 27 and 29, over—

[(B) the tentative minimum tax for the taxable year.]

(3) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) for any taxable year shall not exceed the excess (if any) of the regular tax for the taxable year reduced by the sum of the credits allowable under subpart A and sections 27 and 29. In the case of a taxpayer other than a corporation, such excess shall be further reduced (but not below zero) by the tentative minimum tax for the taxable year.

* * * * * * *

(e) TERMINATION.—This section shall not apply to any property placed in service after December 31, [2004] *2006*.

SEC. 30A. PUERTO RICO ECONOMIC ACTIVITY CREDIT.

(a) * * *

* * * * * * *

(c) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by subsection (a) shall not be allowed against the tax imposed by—

[(1) section 59A (relating to environmental tax),]

[(2)] *(1)* section 531 (relating to the tax on accumulated earnings),

[(3)] *(2)* section 541 (relating to personal holding company tax), or

[(4)] *(3)* section 1351 (relating to recoveries of foreign expropriation losses).

* * * * * * *

Subpart D—Business Related Credits

* * * * * * *

SEC. 38. GENERAL BUSINESS CREDIT.

(a) * * *

* * * * * * *

(c) LIMITATION BASED ON AMOUNT OF TAX.—

[(1) IN GENERAL.—The credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer's net income tax over the greater of—

[(A) the tentative minimum tax for the taxable year, or

[(B) 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000.

For purposes of the preceding sentence, the term "net income tax" means the sum of the regular tax liability and the tax imposed by section 55, reduced by the credits allowable under subparts A and B of this part, and the term "net regular tax liability" means the regular tax liability reduced by the sum of the credits allowable under subparts A and B of this part.]

(1) IN GENERAL.—

(A) CORPORATIONS.—In the case of a corporation, the credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer's net income tax over 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000.

(B) TAXPAYERS OTHER THAN CORPORATIONS.—In the case of a taxpayer other than a corporation, the credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer's net income tax over the greater of—

(i) the tentative minimum tax for the taxable year, or

(ii) 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000.

(C) DEFINITIONS.—For purposes of this paragraph—

(i) the term "net income tax" means the sum of the regular tax liability and the tax imposed by section 55, reduced by the credits allowable under subparts A and B of this part, and

(ii) the term "net regular tax liability" means the regular tax liability reduced by the sum of the credits allowable under subparts A and B of this part.

(2) EMPOWERMENT ZONE EMPLOYMENT CREDIT MAY OFFSET 25 PERCENT OF MINIMUM TAX.—

(A) IN GENERAL.—In the case of the empowerment zone employment credit—

(i) this section and section 39 shall be applied separately with respect to such credit, and

[(ii) for purposes of applying paragraph (1) to such credit

[(I) 75 percent of the tentative minimum tax shall be substituted for the tentative minimum tax under subparagraph (A) thereof, and

[(II) the limitation under paragraph (1) (as modified by subclause (I)) shall be reduced by the credit allowed under subsection (a) for the taxable year (other than the empowerment zone employment credit).]

(ii) for purposes of applying paragraph (1) to such credit—

(I) the applicable limitation under paragraph (1) (as modified by subclause (II) in the case of a taxpayer other than a corporation) shall be reduced

by the credit allowed under subsection (a) for the taxable year (other than the empowerment zone employment credit), and

(II) in the case of a taxpayer other than a corporation, 75 percent of the tentative minimum tax shall be substituted for the tentative minimum tax under subparagraph (B)(i) thereof.

* * * * * * *

(3) SPECIAL RULES.—

(A) MARRIED INDIVIDUALS.—In the case of a husband or wife who files a separate return, the amount specified under [subparagraph (B) of] paragraph (1) shall be $12,500 in lieu of $25,000. This subparagraph shall not apply if the spouse of the taxpayer has no business credit carryforward or carryback to, and has no current year business credit for, the taxable year of such spouse which ends within or with the taxpayer's taxable year.

(B) CONTROLLED GROUPS.—In the case of a controlled group, the $25,000 amount specified under [subparagraph (B) of] paragraph (1) shall be reduced for each component member of such group by apportioning $25,000 among the component members of such group in such manner as the Secretary shall by regulations prescribe. For purposes of the preceding sentence, the term "controlled group" has the meaning given to such term by section 1563(a).

(C) LIMITATIONS WITH RESPECT TO CERTAIN PERSONS.—In the case of a person described in subparagraph (A) or (B) of section 46(e)(1) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990), the $25,000 amount specified under [subparagraph (B) of] paragraph (1) shall equal such person's ratable share (as determined under section 46(e)(2) (as so in effect) of such amount.

(D) ESTATES AND TRUSTS.—In the case of an estate or trust, the $25,000 amount specified under [subparagraph (B) of] paragraph (1) shall be reduced to an amount which bears the same ratio to $25,000 as the portion of the income of the estate or trust which is not allocated to beneficiaries bears to the total income of the estate or trust.

* * * * * * *

SEC. 45. ELECTRICITY PRODUCED FROM CERTAIN RENEWABLE RESOURCES.

(a) * * *

* * * * * * *

(c) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * * * *

(3) QUALIFIED FACILITY.—

(A) WIND FACILITY.—In the case of a facility using wind to produce electricity, the term "qualified facility" means any facility owned by the taxpayer which is originally placed in service after December 31, 1993, and before January 1, [2002] *2004.*

(B) CLOSED-LOOP BIOMASS FACILITY.—In the case of a facility using closed-loop biomass to produce electricity, the term "qualified facility" means any facility owned by the taxpayer which is originally placed in service after December 31, 1992, and before January 1, [2002] *2004*.

(C) POULTRY WASTE FACILITY.—In the case of a facility using poultry waste to produce electricity, the term "qualified facility" means any facility of the taxpayer which is originally placed in service after December 31, 1999, and before January 1, [2002] *2004*.

* * * * * * *

Subpart F—Rules for Computing Work Opportunity Credit

* * * * * * *

SEC. 51. AMOUNT OF CREDIT.

(a) * * *

* * * * * * *

(c) WAGES DEFINED.—For purposes of this subpart—

(1) * * *

* * * * * * *

(4) TERMINATION.—The term "wages" shall not include any amount paid or incurred to an individual who begins work for the employer—

(A) after December 31, 1994, and before October 1, 1996, or

(B) after December 31, [2001] *2003*.

* * * * * * *

SEC. 51A. TEMPORARY INCENTIVES FOR EMPLOYING LONG-TERM FAMILY ASSISTANCE RECIPIENTS.

(a) * * *

* * * * * * *

(f) TERMINATION.—This section shall not apply to individuals who begin work for the employer after December 31, [2001] *2003*.

* * * * * * *

Subpart G—Credit Against Regular Tax for Prior Year Minimum Tax Liability

* * * * * * *

SEC. 53. CREDIT FOR PRIOR YEAR MINIMUM TAX LIABILITY.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this section—

(1) NET MINIMUM TAX

(A) * * *

(B) CREDIT NOT ALLOWED FOR EXCLUSION PREFERENCES.—

(i) * * *

(ii) SPECIFIED ITEMS.—The following are specified in this clause—

(I) the adjustments provided for in subsection [(b)(1)] *(a)(8)* of section 56, and

* * * * * * *

[(iv) CREDIT ALLOWABLE FOR EXCLUSION PREFERENCES OF CORPORATIONS.—In the case of a corporation—

[(I) the preceding provisions of this subparagraph shall not apply, and

[(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii).]

* * * * * * *

PART VI—MINIMUM TAX FOR TAX PREFERENCES

[Sec. 55. Alternative minimum tax imposed.]
Sec. 55. Alternative minimum tax for taxpayers other than corporations.

* * * * * * *

[SEC. 55. ALTERNATIVE MINIMUM TAX IMPOSED.

[(a) GENERAL RULE.—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) NONCORPORATE TAXPAYERS.—

[(i) IN GENERAL.—In the case of a taxpayer other than a corporation, 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.

[(ii) 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.

[(iii) MARRIED INDIVIDUAL FILING SEPARATE RETURN.—In the case of a married individual filing a separate return, clause (i) shall be applied by substituting "$87,500" for "$175,000" each place it appears. For purposes of the preceding sentence, marital status shall be determined under section 7703.

[(B) CORPORATIONS.—In the case of a corporation, the tentative minimum tax for the taxable year is—

[(i) 20 percent of so much of the alternative minimum taxable income for the taxable year as exceeds the exemption amount, reduced by

[(ii) the alternative minimum tax foreign tax credit for the taxable year.]

SEC. 55. ALTERNATIVE MINIMUM TAX FOR TAXPAYERS OTHER THAN CORPORATIONS.

(a) IN GENERAL.—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, clause (i) shall be applied by substituting "$87,500" for "$175,000" each place it appears. For purposes of the preceding sentence, marital status shall be determined under section 7703.

* * * * * * *

(3) MAXIMUM OF TAX ON NET CAPITAL GAIN OF NONCORPORATE TAXPAYERS.—The amount determined under the first sentence of paragraph [(1)(A)(i)] *(1)(A)* shall not exceed the sum of—

(A) * * *

(B) [10] *8* percent of so much of the adjusted net capital gain (or, if less, taxable excess) as does not exceed the amount on which a tax is determined under section 1(h)(1)(B), plus

(C) [20] *18* percent of the adjusted net capital gain (or, if less, taxable excess) in excess of the amount on which tax is determined under subparagraph (B), plus

[In the case of taxable years beginning after December 31, 2000, rules similar to the rules of section 1(h)(2) shall apply for purposes of subparagraphs (B) and (C).] 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)[, the section 936 credit allowable under section 27(b), and the Puerto Rico economic activity

credit under section 30A]. Such term shall not include any increase in tax under section 49(b) or 50(a) or subsection (j) or (k) of section 42.

* * * * * * *

(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].—*The* term "exemption amount" means—

(A) $45,000 [($49,000 in the case of taxable years beginning in 2001, 2002, 2003, and 2004)] *($49,000 in the case of taxable years beginning in 2001, $52,200 in the case of taxable years beginning in 2002 or 2003, and $50,700 in the case of taxable years beginning in 2004)* in the case of—

(i) a joint return, or

(ii) a surviving spouse,

(B) $33,750 [($35,750 in the case of taxable years beginning in 2001, 2002, 2003, and 2004)] *($35,750 in the case of taxable years beginning in 2001, $37,350 in the case of taxable years beginning in 2002 or 2003, and $36,600 in the case of taxable years beginning in 2004)* in the case of an individual who—

(i) is not a married individual, and

(ii) is not a surviving spouse,

[(2) CORPORATIONS.—In the case of a corporation, the term "exemption amount" means $40,000.]

[(3)] *(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 in the case of a taxpayer described in paragraph (1)(A) [or (2)],

* * * * * * *

[(e) EXEMPTION FOR SMALL CORPORATIONS.—

[(1) IN GENERAL.—

[(A) $7,500,000 GROSS RECEIPTS TEST.—The tentative minimum tax of a corporation shall be zero for any taxable year if the corporation's average annual gross receipts for all 3-taxable-year periods ending before such taxable year does not exceed $7,500,000. For purposes of the preceding sentence, only taxable years beginning after December 31, 1993, shall be taken into account.

[(B) $5,000,000 GROSS RECEIPTS TEST FOR FIRST 3-YEAR PERIOD.—Subparagraph (A) shall be applied by substituting "$5,000,000" for "$7,500,000" for the first 3-taxable-year period (or portion thereof) of the corporation which is taken into account under subparagraph (A).

[(C) FIRST TAXABLE YEAR COPORATION IN EXISTENCE.—If such taxable year is the first taxable year that such corporation is in existence, the tentative minimum tax of such corporation for such year shall be zero.

[(D) SPECIAL RULES.—For purposes of this paragraph, the rules of paragraphs (2) and (3) of section 448(c) shall apply.

[(2) PROSPECTIVE APPLICATION OF MINIMUM TAX IF SMALL CORPORATION CEASES TO BE SMALL.—In the case of a corporation whose tentative minimum tax is zero for any prior taxable year by reason of paragraph (1), the application of this part for taxable years beginning with the first taxable year such corporation ceases to be described in paragraph (1) shall be determined with the following modifications:

[(A) Section 56(a)(1) (relating to depreciation) and section 56(a)(5) (relating to pollution control facilities) shall apply only to property placed in service on or after the change date.

[(B) Section 56(a)(2) (relating to mining exploration and development costs) shall apply only to costs paid or incurred on or after the change date.

[(C) Section 56(a)(3) (relating to treatment of long-term contracts) shall apply only to contracts entered into on or after the change date.

[(D) Section 56(a)(4) (relating to alternative net operating loss deduction) shall apply in the same manner as if, in section 56(d)(2), the change date were substituted for "January 1, 1987" and the day before the change date were substituted for "December 31, 1986" each place it appears.

[(E) Section 56(g)(2)(B) (relating to limitation on allowance of negative adjustments based on adjusted current earnings) shall apply only to prior taxable years beginning on or after the change date.

[(F) Section 56(g)(4)(A) (relating to adjustment for depreciation to adjusted current earnings) shall not apply.

[(G) Subparagraphs (D) and (F) of section 56(g)(4) (relating to other earnings and profits adjustments and depletion) shall apply in the same manner as if the day before the change date were substituted for "December 31, 1989" each place it appears therein.

[(3) EXCEPTION.—The modifications in paragraph (2) shall not apply to—

[(A) any item acquired by the corporation in a transaction to which section 381 applies, and

[(B) any property the basis of which in the hands of the corporation is determined by reference to the basis of the property in the hands of the transferor, if such item or property was subject to any provision referred to in paragraph (2) while held by the transferor.

[(4) CHANGE DATE.—For purposes of paragraph (2), the change date is the first day of the first taxable year for which the taxpayer ceases to be described in paragraph (1).

[(5) LIMITATION ON USE OF CREDIT FOR PRIOR YEAR MINIMUM TAX LIABILITY.—In the case of a taxpayer whose tentative minimum tax for any taxable year is zero by reason of paragraph (1), section 53(c) shall be applied for such year by reducing the amount otherwise taken into account under section 53(c)(1) by 25 percent of so much of such amount as exceeds $25,000. Rules similar to the rules of section 38(c)(3)(B) shall apply for purposes of the preceding sentence.]

SEC. 56. ADJUSTMENTS IN COMPUTING ALTERNATIVE MINIMUM TAXABLE INCOME.

[(a) ADJUSTMENTS APPLICABLE TO ALL TAXPAYERS.—] *(a) GENERAL RULES.*—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)] *clauses (ii) and (iii)*, 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)] *clauses (ii) and (iii)* shall continue to apply.

* * * * * * *

(iii) ADDITIONAL ALLOWANCE FOR CERTAIN PROPERTY ACQUIRED AFTER SEPTEMBER 10, 2001, AND BEFORE SEPTEMBER 11, 2004.—The deduction under section 168(k) shall be allowed.

* * * * * * *

[(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.]

* * * * * * *

(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)] *paragraph (2) or (9)* applies) shall be determined on the basis of the treatment prescribed in paragraph (1), (2), [or (5), or subsection (b)(2)] *(5), or (9)*, whichever applies.

* * * * * * *

[(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)] *(8)* LIMITATION ON DEDUCTIONS.—

(A) * * *

* * * * * * *

[(2)] *(9)* CIRCULATION AND RESEARCH AND EXPERIMENTAL EXPENDITURES.—

(A) * * *

* * * * * * *

[(C) SPECIAL RULE FOR PERSONAL HOLDING COMPANIES.—In the case of circulation expenditures described in section 173, the adjustments provided in this paragraph shall

apply also to a personal holding company (as defined in section 542).]

[(D)] *(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 deduction under section 174(a) for expenditures paid or incurred in connection with such activity.

[(3)] *(10)* 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.

[(c) ADJUSTMENTS APPLICABLE TO CORPORATIONS.—In determining the amount of the alternative minimum taxable income of a corporation, the following treatment shall apply:

[(1) ADJUSTMENT FOR ADJUSTED CURRENT EARNINGS.—Alternative minimum taxable income shall be adjusted as provided in subsection (g).

[(2) MERCHANT MARINE CAPITAL CONSTRUCTION FUNDS.—In the case of a capital construction fund established under section 607 of the Merchant Marine Act, 1936 (46 U.S.C. 1177)—

[(A) subparagraphs (A), (B), and (C) of section 7518(c)(1) (and the corresponding provisions of such section 607 shall not apply to—

[(i) any amount deposited in such fund after December 31, 1986, or

[(ii) any earnings (including gains and losses) after December 31, 1986, on amounts in such fund, and

[(B) no reduction in basis shall be made under section 7518(f) (or the corresponding provisions of such section 607 with respect to the withdrawal from the fund of any amount to which subparagraph (A) applies.

For purposes of this paragraph, any withdrawal of deposits or earnings from the fund shall be treated as allocable first to deposits made before (and earnings received or accrued before) January 1, 1987.

[(3) SPECIAL DEDUCTION FOR CERTAIN ORGANIZATIONS NOT ALLOWED.—The deduction determined under section 833(b) shall not be allowed.]

[(d)] *(b)* 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 90 percent of alternate minimum taxable income determined without regard to such deduction, and]

(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 attributable to carrybacks described in clause (ii)(I)), or

(II) 90 percent of alternate minimum taxable income determined without regard to such deduction, plus

(ii) the lesser of—

(I) the amount of such deduction attributable to carrybacks of net operating losses for taxable years ending after September 10, 2001, and before September 11, 2004, or

(II) alternate minimum taxable income determined without regard to such deduction reduced by the amount determined under clause (i), and

* * * * * * *

[(e)] *(c)* 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) * * *

* * * * * * *

[(g) ADJUSTMENTS BASED ON ADJUSTED CURRENT EARNINGS.—

[(1) IN GENERAL.—The alternative minimum taxable income of any corporation for any taxable year shall be increased by 75 percent of the excess (if any) of—

[(A) the adjusted current earnings of the corporation, over

[(B) the alternative minimum taxable income (determined without regard to this subsection and the alternative tax net operating loss deduction).

[(2) ALLOWANCE OF NEGATIVE ADJUSTMENTS.—

[(A) IN GENERAL.—The alternative minimum taxable income for any corporation of any taxable year, shall be reduced by 75 percent of the excess (if any) of—

[(i) the amount referred to in subparagraph (B) of paragraph (1), over

[(ii) the amount referred to in subparagraph (A) of paragraph (1).

[(B) LIMITATION.—The reduction under subparagraph (A) for any taxable year shall not exceed the excess (if any) of—

[(i) the aggregate increases in alternative minimum taxable income under paragraph (1) for prior taxable years, over

[(ii) the aggregate reductions under subparagraph (A) of this paragraph for prior taxable years.

[(3) ADJUSTED CURRENT EARNINGS.—For purposes of this subsection, the term "adjusted current earnings" means the alternative minimum taxable income for the taxable year—

[(A) determined with the adjustments provided in paragraph (4), and

[(B) determined without regard to this subsection and the alternative tax net operating loss deduction.

[(4) ADJUSTMENTS.—In determining adjusted current earnings, the following adjustments shall apply:

[(A) DEPRECIATION.—

[(i) PROPERTY PLACED IN SERVICE AFTER 1989.—The depreciation deduction with respect to any property placed in service in a taxable year beginning after 1989 shall be determined under the alternative system of section 168(g). The preceding sentence shall not apply to any property placed in service after December 31, 1993, and the depreciation deduction with respect to such property shall be determined under the rules of subsection (a)(1)(A).

[(ii) PROPERTY TO WHICH NEW ACRS SYSTEM APPLIES.—In the case of any property to which the amendments made by section 201 of the Tax Reform Act of 1986 apply and which is placed in service in a taxable year beginning before 1990, the depreciation deduction shall be determined—

[(I) by taking into account the adjusted basis of such property (as determined for purposes of computing alternative minimum taxable income) as of the close of the last taxable year beginning before January 1, 1990, and

[(II) by using the straight-line method over the remainder of the recovery period applicable to such property under the alternative system of section 168(g).

[(iii) PROPERTY TO WHICH ORIGINAL ACRS SYSTEM APPLIES.—In the case of any property to which section 168 (as in effect on the day before the date of the enactment of the Tax Reform Act of 1986 and without regard to subsection (d)(1)(A)(ii) thereof) applies and which is placed in service in a taxable year beginning before 1990, the depreciation deduction shall be determined—

[(I) by taking into account the adjusted basis of such property (as determined for purposes of computing the regular tax) as of the close of the last taxable year beginning before January 1, 1990, and

[(II) by using the straight line method over the remainder of the recovery period which would apply to such property under the alternative system of section 168(g).

[(iv) PROPERTY PLACED IN SERVICE BEFORE 1981.—In the case of any property not described in clause (i), (ii), or (iii), the amount allowable as depreciation or amortization with respect to such property shall be determined in the same manner as for purposes of computing taxable income.

[(v) SPECIAL RULE FOR CERTAIN PROPERTY.—In the case of any property described in paragraph (1), (2), (3), or (4) of section 168(f), the amount of depreciation allowable for purposes of the regular tax shall be treated as the amount allowable under the alternative system of section 168(g).

[(B) INCLUSION OF ITEMS INCLUDED FOR PURPOSES OF COMPUTING EARNINGS AND PROFITS.—

[(i) IN GENERAL.—In the case of any amount which is excluded from gross income for purposes of computing alternative minimum taxable income but is taken into account in determining the amount of earnings and profits—

[(I) such amount shall be included in income in the same manner as if such amount were includible in gross income for purposes of computing alternative minimum taxable income, and

[(II) the amount of such income shall be reduced by any deduction which would have been allowable in computing alternative minimum taxable income if such amount were includible in gross income.

The preceding sentence shall not apply in the case of any amount excluded from gross income under section 108 (or the corresponding provisions of prior law) or under section 114. In the case of any insurance company taxable under section 831(b), this clause shall not apply to any amount not described in section 834(b).

[(ii) INCLUSION OF BUILDUP IN LIFE INSURANCE CONTRACTS.—In the case of any life insurance contract—

[(I) the income on such contract (as determined under section 7702(g)) for any taxable year shall be treated as includible in gross income for such year, and

[(II) there shall be allowed as a deduction that portion of any premium which is attributable to insurance coverage.

[(C) DISALLOWANCE OF ITEMS NOT DEDUCTIBLE IN COMPUTING EARNINGS AND PROFITS.—

[(i) IN GENERAL.—A deduction shall not be allowed for any item if such item would not be deductible for any taxable year for purposes of computing earnings and profits.

[(ii) SPECIAL RULE FOR CERTAIN DIVIDENDS.—

[(I) IN GENERAL.—Clause (i) shall not apply to any deduction allowable under section 243 or 245 for any dividend which is a 100-percent dividend or which is received from a 20-percent owned corporation (as defined in section 243(c)(2)), but only to the extent such dividend is attributable to income of the paying corporation which is subject to tax under this chapter (determined after the application of sections 30A, 936 (including subsections (a)(4), (i) and (j) thereof) and 921).

[(II) 100-PERCENT DIVIDEND.—For purposes of subclause (I), the term "100 percent dividend" means any dividend if the percentage used for purposes of determining the amount allowable as a deduction under section 243 or 245 with respect to such dividend is 100 percent.

[(iii) TREATMENT OF TAXES ON DIVIDENDS FROM 936 CORPORATIONS.—

[(I) IN GENERAL.—For purposes of determining the alternative minimum foreign tax credit, 75 percent of any withholding or income tax paid to a possession of the United States with respect to dividends received from a corporation eligible for the credit provided by section 936 shall be treated as a tax paid to a foreign country by the corporation receiving the dividend.

[(II) LIMITATION.—If the aggregate amount of the dividends referred to in subclause (I) for any taxable year exceeds the excess referred to in paragraph (1), the amount treated as tax paid to a foreign country under subclause (I) shall not exceed the amount which would be so treated without regard to this subclause multiplied by a fraction the numerator of which is the excess referred to in paragraph (1) and the denominator of which is the aggregate amount of such dividends.

[(III) TREATMENT OF TAXES IMPOSED ON 936 CORPORATION.—For purposes of this clause, taxes paid by any corporation eligible for the credit provided by section 936 to a possession of the United States shall be treated as a withholding tax paid with respect to any dividend paid by such corporation to the extent such taxes would be treated as paid by the corporation receiving the dividend under rules similar to the rules of section 902 (and the amount of any such dividend shall be increased by the amount so treated).

[(IV) SEPARATE APPLICATION OF FOREIGN TAX CREDIT LIMITATIONS.—In determining the alternative minimum foreign tax credit, section 904(d) shall be applied as if dividends from a corporation eligible for the credit provided by section 936 were a separate category of income referred to in a subparagraph of section 904(d)(1).

[(V) COORDINATION WITH LIMITATION ON 936 CREDIT.—Any reference in this clause to a dividend received from a corporation eligible for the credit provided by section 936 shall be treated as a reference to the portion of any such dividend for which the dividends received deduction is disallowed under clause (i) after the application of clause (ii)(I).

[(VI) APPLICATIONS TO SECTION 30A CORPORATIONS.—References in this clause to section 936 shall be treated as including references to section 30A.

[(iv) SPECIAL RULE FOR CERTAIN DIVIDENDS RECEIVED BY CERTAIN COOPERATIVES.—In the case of a cooperative described in section 927(a)(4), clause (i) shall not apply to any amount allowable as a deduction under section 245(c).

[(D) CERTAIN OTHER EARNINGS AND PROFITS ADJUSTMENTS.—

[(i) INTANGIBLE DRILLING COSTS.—The adjustments provided in section 312(n)(2)(A) shall apply in the case of amounts paid or incurred in taxable years beginning after December 31, 1989. In the case of a taxpayer other than an integrated oil company (as defined in section 291(b)(4), in the case of any oil or gas well, this clause shall not apply in the case of amounts paid or incurred in taxable years beginning after December 31, 1992.

[(ii) CERTAIN AMORTIZATION PROVISIONS NOT TO APPLY.—Sections 173 and 248 shall not apply to expenditures paid or incurred in taxable years beginning after December 31, 1989.

[(iii) LIFO INVENTORY ADJUSTMENTS.—The adjustments provided in section 312(n)(4) shall apply, but only with respect to taxable years beginning after December 31, 1989.

[(iv) INSTALLMENT SALES.—In the case of any installment sale in a taxable year beginning after December 31, 1989, adjusted current earnings shall be computed as if the corporation did not use the installment method. The preceding sentence shall not apply to the applicable percentage (as determined under section 453A) of the gain from any installment sale with respect to which section 453A(a)(1) applies.

[(E) DISALLOWANCE OF LOSS ON EXCHANGE OF DEBT POOLS.—No loss shall be recognized on the exchange of any pool of debt obligations for another pool of debt obligations having substantially the same effective interest rates and maturities.

[(F) DEPLETION.—

[(i) IN GENERAL.—The allowance for depletion with respect to any property placed in service in a taxable year beginning after December 31, 1989, shall be cost depletion determined under section 611.

[(ii) EXCEPTION FOR INDEPENDENT OIL AND GAS PRODUCERS AND ROYALTY OWNERS.—In the case of any taxable year beginning after December 31, 1992, clause (i) (and subparagraph (C)(i)) shall not apply to any deduction for depletion computed in accordance with section 613A(c).

[(G) TREATMENT OF CERTAIN OWNERSHIP CHANGES.—If—

[(i) there is an ownership change (within the meaning of section 382) in a taxable year beginning after 1989 with respect to any corporation, and

[(ii) there is a net unrealized built-in loss (within the meaning of section 382(h)) with respect to such corporation, then the adjusted basis of each asset of

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

[(H) ADJUSTED BASIS.—The adjusted basis of any property with respect to which an adjustment under this paragraph applies shall be determined by applying the treatment prescribed in this paragraph.

[(I) TREATMENT OF CHARITABLE CONTRIBUTIONS.—Notwithstanding subparagraphs (B) and (C), no adjustment related to the earnings and profits effects of any charitable contribution shall be made in computing adjusted current earnings.

[(5) OTHER DEFINITIONS.—For purposes of paragraph (4)—

[(A) EARNINGS AND PROFITS.—The term "earnings and profits" means earnings and profits computed for purposes of subchapter C.

[(B) TREATMENT OF ALTERNATIVE MINIMUM TAXABLE INCOME.—The treatment of any item for purposes of computing alternative minimum taxable income shall be determined without regard to this subsection.

[(6) EXCEPTION FOR CERTAIN CORPORATIONS.—This subsection shall not apply to any S corporation, regulated investment company, real estate investment trust, REMIC, or FASIT.]

SEC. 57. ITEMS OF TAX PREFERENCE.

(a) GENERAL RULE.—For purposes of this part, the items of tax preference determined under this section are—

(1) * * *

(2) INTANGIBLE DRILLING COSTS.—

(A) * * *

* * * * * * *

(E) EXCEPTION [FOR INDEPENDENT PRODUCERS].—In the case of any oil or gas well—

[(i) IN GENERAL.—In the case of any taxable year beginning after December 31, 1992, this paragraph shall not apply to any taxpayer which is not an integrated oil company (as defined in section 291(b)(4)).]

(i) IN GENERAL.—This paragraph shall not apply to any taxable year beginning after December 31, 1992.

* * * * * * *

(7) EXCLUSION FOR GAINS ON SALE OF CERTAIN SMALL BUSINESS STOCK.—An amount equal to [42] *28* percent of the amount excluded from gross income for the taxable year under section 1202. [In the case of stock the holding period of which begins after December 31, 2000 (determined with the application of the last sentence of section 1(h)(2)(B)), the preceding sentence shall be applied by substituting "28 percent" for "42 percent".]

* * * * * * *

SEC. 58. DENIAL OF CERTAIN LOSSES.

(a) DENIAL OF FARM LOSS.—

(1) * * *

* * * * * * *

[(3) APPLICATION TO PERSONAL SERVICE CORPORATIONS.—For purposes of paragraph (1), a personal service corporation (within the meaning of section 469(j)(2)) shall be treated as a taxpayer other than a corporation.]

[(4)] *(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.

* * * * * * *

SEC. 59. OTHER DEFINITIONS AND SPECIAL RULES.

(a) * * *

[(b) MINIMUM TAX NOT TO APPLY TO INCOME ELIGIBLE FOR CREDITS UNDER SECTION 30A OR 936.—In the case of any corporation for which a credit is allowable for the taxable year under section 30A or 936, alternative minimum taxable income shall not include any income with respect to which a credit is determined under section 30A or 936.]

[(c)] *(b)* TREATMENT OF ESTATES AND TRUSTS.—In the case of any estate or trust, the alternative minimum taxable income of such estate or trust and any beneficiary thereof shall be determined by applying part I of subchapter J with the adjustments provided in this part.

[(d)] *(c)* APPORTIONMENT OF DIFFERENTLY TREATED ITEMS IN CASE OF CERTAIN ENTITIES.—

(1) * * *

* * * * * * *

[(e)] *(d)* OPTIONAL 10-YEAR WRITE-OFF OF CERTAIN TAX PREFERENCES.—

(1) * * *

(2) QUALIFIED EXPENDITURE.—For purposes of this subsection, the term "qualified expenditure" means any amount which, but for an election under this subsection, would have been allowable as a deduction [(determined without regard to section 291)] for the taxable year in which paid or incurred under—

(A) * * *

* * * * * * *

[(f) COORDINATION WITH SECTION 291.—Except as otherwise provided in this part, section 291 (relating to cutback of corporate preferences) shall apply before the application of this part.]

[(g)] *(e)* TAX BENEFIT RULE.—The Secretary may prescribe regulations under which differently treated items shall be properly adjusted where the tax treatment giving rise to such items will not result in the reduction of the taxpayer's regular tax for the taxable year for which item is taken into account or for any other taxable year.

[(h)] *(f)* COORDINATION WITH CERTAIN LIMITATIONS.—The limitations of sections 704(d), 465, and 1366(d) (and such other provisions as may be specified in regulations) shall be applied for purposes of computing the alternative minimum taxable income of the taxpayer

for the taxable year with the adjustments of sections 56, 57, and 58.

[(i)] *(g)* SPECIAL RULE FOR AMOUNTS TREATED AS TAX PREFERENCE.—For purposes of this subtitle (other than this part), any amount shall not fail to be treated as wholly exempt from tax imposed by this subtitle solely by reason of being included in alternative minimum taxable income.

[(j)] *(h)* TREATMENT OF UNEARNED INCOME OF MINOR CHILDREN.—

(1) IN GENERAL.—In the case of a child to whom section 1(g) applies, the exemption amount for purposes of section 55 shall not exceed the sum of—

* * * * * * *

[PART VII—ENVIRONMENTAL TAX

[59A. Environmental tax.

[SEC. 59A. ENVIRONMENTAL TAX.

[(a) IMPOSITION OF TAX.—In the case of a corporation, there is hereby imposed (in addition to any other tax imposed by this subtitle) a tax equal to 0.12 percent of the excess of—

[(1) the modified alternative minimum taxable income of such corporation for the taxable year, over

[(2) $2,000,000.

[(b) MODIFIED ALTERNATIVE MINIMUM TAXABLE INCOME.—For purposes of this section, the term "modified alternative minimum taxable income" means alternative minimum taxable income (as defined in section 55(b)(2) but determined without regard to—

[(1) the alternative tax net operating loss deduction (as defined in section 56(d)) and

[(2) the deduction allowed under section 164(a)(5).

[(c) EXCEPTION FOR RIC'S AND REIT'S.—The tax imposed by subsection (a) shall not apply to—

[(1) a regulated investment company to which part I of subchapter M applies, and

[(2) a real estate investment trust to which part II of subchapter M applies.

[(d) SPECIAL RULES.—

[(1) SHORT TAXABLE YEARS.—The application of this section to taxable years of less than 12 months shall be in accordance with regulations prescribed by the Secretary.

[(2) SECTION 15 NOT TO APPLY.—Section 15 shall not apply to the tax imposed by this section.

[(e) Application of Tax.—

[(1) IN GENERAL.—The tax imposed by this section shall apply to taxable years beginning after December 31, 1986, and before January 1, 1996.

[(2) EARLIER TERMINATION.—The tax imposed by this section shall not apply to taxable years—

[(A) beginning during a calendar year during which no tax is imposed under section 4611(a) by reason of paragraph (2) of section 4611(e), and

[(B) beginning after the calendar year which includes the termination date under paragraph (3) of section 4611(e).]

Subchapter B—Computation of Taxable Income

* * * * * * *

PART II—ITEMS SPECIFICALLY INCLUDED IN GROSS INCOME

* * * * * * *

SEC. 72. ANNUITIES; CERTAIN PROCEEDS OF ENDOWMENT AND LIFE INSURANCE CONTRACTS.

(a) * * *

* * * * * * *

(t) 10-PERCENT ADDITIONAL TAX ON EARLY DISTRIBUTIONS FROM QUALIFIED RETIREMENT PLANS.—

(1) * * *

(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) * * *

* * * * * * *

(D) DISTRIBUTIONS TO UNEMPLOYED INDIVIDUALS FOR HEALTH INSURANCE PREMIUMS.—

(i) * * *

* * * * * * *

(iv) SPECIAL RULES FOR INDIVIDUALS RECEIVING UNEMPLOYMENT COMPENSATION AFTER SEPTEMBER 10, 2001, AND BEFORE JANUARY 1, 2003.—In the case of an individual who receives unemployment compensation for 4 consecutive weeks after September 10, 2001, and before January 1, 2003—

(I) clause (i) shall apply to distributions from all qualified retirement plans (as defined in section 4974(c)), and

(II) such 4 consecutive weeks shall be substituted for the 12 consecutive weeks referred to in subclause (I) of clause (i).

* * * * * * *

PART III—ITEMS SPECIFICALY EXCLUDED FROM GROSS INCOME

* * * * * * *

SEC. 108. INCOME FROM DISCHARGE OF INDEBTEDNESS.

(a) * * *

* * * * * * *

(d) MEANING OF TERMS; SPECIAL RULES RELATING TO CERTAIN PROVISIONS.—

(1) * * *

* * * * * * *

(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.*

* * * * * * *

PART VI—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS

* * * * * * *

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) * * *

* * * * * * *

[(5) THE ENVIRONMENTAL TAX IMPOSED BY SECTION 59A.—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.]

* * * * * * *

SEC. 168. ACCELERATED COST RECOVERY SYSTEM.

(a) * * *

(b) APPLICABLE DEPRECIATION METHOD.—For purposes of this section—

(1) * * *

* * * * * * *

(3) PROPERTY TO WHICH STRAIGHT LINE METHOD APPLIES.—The applicable depreciation method shall be the straight line method in the case of the following property:

(A) * * *

* * * * * * *

(G) Qualified leasehold improvement property described in subsection (e)(6).

* * * * * * *

(e) CLASSIFICATION OF PROPERTY.—For purposes of this section—

(1) * * *

* * * * * * *

(3) CLASSIFICATION OF CERTAIN PROPERTY.—

(A) * * *

* * * * * * *

(E) 15-YEAR PROPERTY.—The term "15-year property" includes—

(i) any municipal wastewater treatment plant,

(ii) any telephone distribution plant and comparable equipment used for 2-way exchange of voice and data communications, [and]

(iii) any section 1250 property which is a retail motor fuels outlet (whether or not food or other convenience items are sold at the outlet)[.], *and*

(iv) any qualified leasehold improvement property.

* * * * * * *

(6) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY.—

(A) IN GENERAL.—The term "qualified leasehold improvement property" means any improvement to an interior portion of a building which is nonresidential real property if—

(i) such improvement is made under or pursuant to a lease (as defined in subsection (h)(7))—

(I) by the lessee (or any sublessee) of such portion, or

(II) by the lessor of such portion,

(ii) such portion is to be occupied exclusively by the lessee (or any sublessee) of such portion, and

(iii) such improvement is placed in service more than 3 years after the date the building was first placed in service.

(B) CERTAIN IMPROVEMENTS NOT INCLUDED.—Such term shall not include any improvement for which the expenditure is attributable to—

(i) the enlargement of the building,

(ii) any elevator or escalator,

(iii) any structural component benefiting a common area, and

(iv) the internal structural framework of the building.

(C) DEFINITIONS AND SPECIAL RULES.—For purposes of this paragraph—

(i) COMMITMENT TO LEASE TREATED AS LEASE.—A commitment to enter into a lease shall be treated as a lease, and the parties to such commitment shall be treated as lessor and lessee, respectively.

(ii) RELATED PERSONS.—A lease between related persons shall not be considered a lease. For purposes of the preceding sentence, the term "related persons" means—

(I) members of an affiliated group (as defined in section 1504), and

(II) persons having a relationship described in subsection (b) of section 267; except that, for purposes of this clause, the phrase "80 percent or more" shall be substituted for the phrase "more than 50 percent" each place it appears in such subsection.

(D) IMPROVEMENTS MADE BY LESSOR.—

(i) IN GENERAL.—In the case of an improvement made by the person who was the lessor of such improvement when such improvement was placed in service, such improvement shall be qualified leasehold im-

provement property (if at all) only so long as such improvement is held by such person.

(ii) EXCEPTION FOR CHANGES IN FORM OF BUSINESS.—Property shall not cease to be qualified leasehold improvement property under clause (i) by reason of—

(I) death,

(II) a transaction to which section 381(a) applies, or

(III) a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as qualified leasehold improvement property and the taxpayer retains a substantial interest in such trade or business.

* * * * * * *

(g) ALTERNATIVE DEPRECIATION SYSTEM FOR CERTAIN PROPERTY

(1) * * *

* * * * * * *

(3) SPECIAL RULES FOR DETERMINING CLASS LIFE.—

(A) * * *

(B) SPECIAL RULE FOR CERTAIN PROPERTY ASSIGNED TO CLASSES.—For purposes of paragraph (2), in the case of property described in any of the following subparagraphs of subsection (e)(3), the class life shall be determined as follows:

If property is described in subparagraph:	**The class life is:**
(A)(ii)	4
(B)(ii)	5
(B)(iii)	9.5
(C)(i)	10
(D)(i)	15
(D)(ii)	20
(E)(i)	24
(E)(ii)	24
(E)(iii)	20
(E)(iv)	*15*

* * * * * * *

(k) SPECIAL ALLOWANCE FOR CERTAIN PROPERTY ACQUIRED AFTER SEPTEMBER 10, 2001, AND BEFORE SEPTEMBER 11, 2004.—

(1) ADDITIONAL ALLOWANCE.—In the case of any qualified property—

(A) the depreciation deduction provided by section 167(a) for the taxable year in which such property is placed in service shall include an allowance equal to 30 percent of the adjusted basis of the qualified property, and

(B) the adjusted basis of the qualified property shall be reduced by the amount of such deduction before computing the amount otherwise allowable as a depreciation deduction under this chapter for such taxable year and any subsequent taxable year.

(2) QUALIFIED PROPERTY.—For purposes of this subsection—

(A) IN GENERAL.—The term "qualified property" means property—

(i)(I) to which this section applies which has a recovery period of 20 years or less or which is water utility property, or

(II) which is computer software (as defined in section 167(f)(1)(B)) for which a deduction is allowable under section 167(a) without regard to this subsection,

(ii) the original use of which commences with the taxpayer after September 10, 2001,

(iii) which is—

(I) acquired by the taxpayer after September 10, 2001, and before September 11, 2004, but only if no written binding contract for the acquisition was in effect before September 11, 2001, or

(II) acquired by the taxpayer pursuant to a written binding contract which was entered into after September 10, 2001, and before September 11, 2004, and

(iv) which is placed in service by the taxpayer before January 1, 2005.

(B) EXCEPTIONS.—

(i) ALTERNATIVE DEPRECIATION PROPERTY.—The term "qualified property" shall not include any property to which the alternative depreciation system under subsection (g) applies, determined—

(I) without regard to paragraph (7) of subsection (g) (relating to election to have system apply), and

(II) after application of section 280F(b) (relating to listed property with limited business use).

(ii) ELECTION OUT.—If a taxpayer makes an election under this clause with respect to any class of property for any taxable year, this subsection shall not apply to all property in such class placed in service during such taxable year.

(iii) REPAIRED OR RECONSTRUCTED PROPERTY.—Except as otherwise provided in regulations, the term "qualified property" shall not include any repaired or reconstructed property.

(iv) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY.—The term "qualified property" shall not include any qualified leasehold improvement property (as defined in section 168(e)(6)).

(C) SPECIAL RULES RELATING TO ORIGINAL USE.—

(i) SELF-CONSTRUCTED PROPERTY.—In the case of a taxpayer manufacturing, constructing, or producing property for the taxpayer's own use, the requirements of clause (iii) of subparagraph (A) shall be treated as met if the taxpayer begins manufacturing, constructing, or producing the property after September 10, 2001, and before September 11, 2004.

(ii) SALE-LEASEBACKS.—For purposes of subparagraph (A)(ii), if property—

(I) is originally placed in service after September 10, 2001, by a person, and

(II) is sold and leased back by such person within 3 months after the date such property was originally placed in service,

such property shall be treated as originally placed in service not earlier than the date on which such property is used under the leaseback referred to in subclause (II).

(D) COORDINATION WITH SECTION 280F.—For purposes of section 280F—

(i) AUTOMOBILES.—In the case of a passenger automobile (as defined in section 280F(d)(5)) which is qualified property, the Secretary shall increase the limitation under section 280F(a)(1)(A)(i) by $4,600.

(ii) LISTED PROPERTY.—The deduction allowable under paragraph (1) shall be taken into account in computing any recapture amount under section 280F(b)(2).

* * * * * * *

SEC. 172. NET OPERATING LOSS DEDUCTION.

(a) * * *

(b) NET OPERATING CARRYBACKS AND CARRYOVERS.—

(1) YEARS TO WHICH LOSS MAY BE CARRIED.—

(A) * * *

* * * * * * *

(H) In the case of a taxpayer which has a net operating loss for any taxable year ending after September 10, 2001, and before September 11, 2004, subparagraph (A)(i) shall be applied by substituting "5" for "2" and subparagraph (F) shall not apply.

* * * * * * *

(j) ELECTION TO DISREGARD 5-YEAR CARRYBACK FOR CERTAIN NET OPERATING LOSSES.—Any taxpayer entitled to a 5-year carryback under subsection (b)(1)(H) from any loss year may elect to have the carryback period with respect to such loss year determined without regard to subsection (b)(1)(H). 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. Such election, once made for any taxable year, shall be irrevocable for such taxable year.

[(j)**]** *(k)* CROSS REFERENCES

(1) * * *

* * * * * * *

SEC. 173. CIRCULATION EXPENDITURES.

(a) * * *

(b) CROSS REFERENCE

For election of 3-year amortization of expenditures allowable as a deduction under subsection (a), see section [59(e)] *59(d)*.

SEC. 174. RESEARCH AND EXPERIMENTAL EXPENDITURES.

(a) * * *

* * * * * * *

(f) CROSS REFERENCES.—

(1) * * *

(2) For election of 10-year amortization of expenditures allowable as a deduction under subsection (a), see section [59(e)] *59(d)*.

* * * * * * *

SEC. 179. ELECTION TO EXPENSE CERTAIN DEPRECIABLE BUSINESS ASSETS.

(a) * * *

(b) LIMITATIONS.—

(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

[If the taxable year begins in:	**The applicable amount is:**
1997	18,000
1998	18,500
1999	19,000
2000	20,000
2001 or 2002	24,000
2003 or thereafter	25,000]
If the taxable year begins in:	***The applicable amount is:***
2001	*$24,000*
2002 or 2003	*$35,000*
2004 or thereafter	*$25,000.*

(2) REDUCTION IN LIMITATION.—The limitation under paragraph (1) for any taxable year shall be reduced (but not below zero) by the amount by which the cost of section 179 property placed in service during such taxable year exceeds $200,000 *($325,000 in the case of taxable years beginning during 2002 or 2003)*.

* * * * * * *

SEC. 179A. DEDUCTION FOR CLEAN-FUEL VEHICLES AND CERTAIN REFUELING PROPERTY.

(a) * * *

(b) LIMITATIONS.—

(1) QUALIFIED CLEAN-FUEL VEHICLE PROPERTY.—

(A) * * *

(B) PHASEOUT.—In the case of any qualified clean-fuel vehicle property placed in service after December 31, [2001] *2003*, the limit otherwise applicable under subparagraph (A) shall be reduced by—

(i) 25 percent in the case of property placed in service in calendar year [2002] *2004*,

(ii) 50 percent in the case of property placed in service in calendar year [2003] *2005*, and

(iii) 75 percent in the case of property placed in service in calendar year [2004] *2006*.

* * * * * * *

(f) TERMINATION.—This section shall not apply to any property placed in service after December 31, [2004] *2006*.

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PART VII—ADDITIONAL ITEMIZED DEDUCTIONS FOR INDIVIDUALS

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SEC. 220. ARCHER MSAS.

(a) * * *

* * * * * * *

(i) LIMITATION ON NUMBER OF TAXPAYERS HAVING ARCHER MSAS.—

(1) * * *

(2) CUT-OFF YEAR.—For purposes of paragraph (1), the term "cut-off year" means the earlier of

(A) calendar year [2002] *2003*, or

(B) the first calendar year before [2002] *2003* 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) * * *

(B) SPECIAL RULE FOR CUT-OFF YEARS BEFORE [2002] *2003*.—In the case of a cut-off year before [2002] *2003*—

(i) * * *

* * * * * * *

(j) DETERMINATION OF WHETHER NUMERICAL LIMITS ARE EXCEEDED.—

(1) * * *

(2) DETERMINATION OF WHETHER LIMIT EXCEEDED FOR [1998, 1999, OR 2001] *1998, 1999, 2001, OR 2002*.—

(A) IN GENERAL.—The numerical limitation for [1998, 1999, or 2001] *1998, 1999, 2001, or 2002* 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, or 2001] *1998, 1999, 2001, or 2002* is also exceeded if the sum of—

(i) * * *

* * * * * * *

(4) REPORTING BY MSA TRUSTEES.—

(A) IN GENERAL.—Not later than August 1 of 1997, 1998, 1999, [and 2001] *2001, and 2002* 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) * * *

* * * * * * *

PART IX—ITEMS NOT DEDUCTABLE

* * * * * * *

SEC. 263. CAPITAL EXPENDITURES.

(a) * * *

* * * * * * *

(c) INTANGIBLE DRILLING AND DEVELOPMENT COSTS IN THE CASE OF OIL AND GAS WELLS AND GEOTHERMAL WELLS.—Notwithstanding subsection (a), and except as provided in subsection (i), regulations shall be prescribed by the Secretary under this subtitle corresponding to the regulations which granted the option to deduct as expenses intangible drilling and development costs in the case of oil and gas wells and which were recognized and approved by the Congress in House Concurrent Resolution 50, Seventy-ninth Congress. Such regulations shall also grant the option to deduct as expenses intangible drilling and development costs in the case of wells drilled for any geothermal deposit (as defined in section 613(e)(2)) to the same extent and in the same manner as such expenses are deductible in the case of oil and gas wells. This subsection shall not apply with respect to any costs to which any deduction is allowed under section [59(e)] *59(d)* or 291.

* * * * * * *

SEC. 263A. CAPITALIZATION AND INCLUSION IN INVENTORY COSTS OF CERTAIN EXPENSES.

(a) * * *

* * * * * * *

(c) GENERAL EXCEPTIONS

(1) * * *

* * * * * * *

(6) COORDINATION WITH SECTION [59(E)] *59(D)*.—Paragraphs (2) and (3) shall apply to any amount allowable as a deduction under section [59(e)] *59(d)* for qualified expenditures described in subparagraphs (B), (C), (D), and (E) of paragraph (2) thereof.

* * * * * * *

SEC. 275. CERTAIN TAXES.

(a) GENERAL RULE.—No deduction shall be allowed for the following taxes:

(1) * * *

* * * * * * *

Paragraph (1) shall not apply to any taxes to the extent such taxes are allowable as a deduction under section 164(f). [Paragraph (1) shall not apply to the tax imposed by section 59A.] A rule similar to the rule of section 943(d) shall apply for purposes of paragraph (4)(C)

* * * * * * *

SEC. 280F. LIMITATION ON DEPRECIATION FOR LUXURY AUTOMOBILES; LIMITATION WHERE CERTAIN PROPERTY USED FOR PERSONAL PURPOSES.

(a) LIMITATION ON AMOUNT OF DEPRECIATION FOR LUXURY AUTOMOBILES.—

(1) DEPRECIATION.—

(A) * * *

* * * * * * *

(C) SPECIAL RULE FOR CERTAIN CLEAN-FUEL PASSENGER AUTOMOBILES.—

(i) * * *

* * * * * * *

(iii) APPLICATION OF SUBPARAGRAPH.—This subparagraph shall apply to property placed in service after August 5, 1997, and before January 1, 2007.

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Subchapter C—Corporate Distributions and Adjustments

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PART V—CARRYOVERS

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SEC. 382. LIMITATION ON NET OPERATING LOSS CARRYFORWARDS AND CERTAIN BUILT-IN LOSSES FOLLOWING OWNERSHIP CHANGE.

(a) * * *

* * * * * * *

(l) CERTAIN ADDITIONAL OPERATING RULES.—For purposes of this section—

(1) * * *

* * * * * * *

[(7) COORDINATION WITH ALTERNATIVE MINIMUM TAX.—The Secretary shall by regulation provide for the application of this section to the alternative tax net operating loss deduction under section 56(d).**]**

[(8)**]** *(7)* PREDECESSOR AND SUCCESSOR ENTITIES.—Except as provided in regulations, any entity and any predecessor or successor entities of such entity shall be treated as 1 entity.

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Subchapter E—Accounting Periods and Methods of Accounting

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PART II—METHODS OF ACCOUNTING

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Subpart A—Methods of Accounting in General

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SEC. 448. LIMITATION ON USE OF CASH METHOD OF ACCOUNTING.

(a) * * *

* * * * * * *

(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

[(5) SPECIAL RULE FOR SERVICES.—In the case of any person using an accrual method of accounting with respect to amounts to be received for the performance of services by such person, such person shall not be required to accrue any portion of such amounts which (on the basis of experience) will not be collected. This paragraph shall not apply to any amount if interest is required to be paid on such amount or there is any penalty for failure to timely pay such amount.]

(5) SPECIAL RULE FOR CERTAIN SERVICES.—

(A) IN GENERAL.—In the case of any person using an accrual method of accounting with respect to amounts to be received for the performance of services by such person, such person shall not be required to accrue any portion of such amounts which (on the basis of such person's experience) will not be collected if—

(i) such services are in fields referred to in paragraph (2)(A), or

(ii) such person meets the gross receipts test of subsection (c) for all prior taxable years.

(B) EXCEPTION.—This paragraph shall not apply to any amount if interest is required to be paid on such amount or there is any penalty for failure to timely pay such amount.

(C) REGULATIONS.—The Secretary shall prescribe regulations to permit taxpayers to determine amounts referred to in subparagraph (A) using computations or formulas which, based on experience, accurately reflect the amount of income that will not be collected by such person. A taxpayer may adopt, or request consent of the Secretary to change to, a computation or formula that clearly reflects the taxpayer's experience. A request under the preceding sentence shall be approved only if such computation or formula clearly reflects the taxpayer's experience.

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Subchapter I—Natural Resources

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PART I—DEDUCTIONS

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SEC. 613A. LIMITATIONS ON PERCENTAGE DEPLETION IN CASE OF OIL AND GAS WELLS.

(a) * * *

* * * * * * *

(c) EXEMPTION FOR INDEPENDENT PRODUCERS AND ROYALTY OWNERS.—

(1) * * *

* * * * * * *

(6) OIL AND NATURAL GAS PRODUCED FROM MARGINAL PROPERTIES.—

(A) * * *

* * * * * * *

(H) TEMPORARY SUSPENSION OF TAXABLE INCOME LIMIT WITH RESPECT TO MARGINAL PRODUCTION.—The second sentence of subsection (a) of section 613 shall not apply to so much of the allowance for depletion as is determined under subparagraph (A) for any taxable year beginning after December 31, 1997, and before January 1, **[**2002**]** *2004*.

* * * * * * *

SEC. 616. DEVELOPMENT EXPENDITURES.

(a) * * *

* * * * * * *

(e) CROSS REFERENCE.—

For election of 10-year amortization of expenditures allowable as a deduction under subsection (a), see section [59(e)] ***59(d)*****.**

SEC. 617. DEDUCTION AND RECAPTURE OF CERTAIN MINING EXPLORATION EXPENDITURES.

(a) * * *

* * * * * * *

(i) CROSS REFERENCE.—

For election of 10-year amortization of expenditures allowable as a deduction under this section, see section [59(e)] ***59(d)*****.**

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Subchapter L—Insurance Companies

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PART I—LIFE INSURANCE COMPANIES

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Subpart D—Accounting, Allocation, and Foreign Provisions

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SEC. 815. DISTRIBUTIONS TO SHAREHOLDERS FROM PRE-1984 POLICYHOLDERS SURPLUS ACCOUNT.

(a) * * *

* * * * * * *

(c) SHAREHOLDERS SURPLUS ACCOUNT.—

(1) * * *

(2) ADDITIONS TO ACCOUNT.—The amount added to the shareholders surplus account for any taxable year beginning after December 31, 1983, shall be the excess of—

(A) * * *

* * * * * * *

[If for any taxable year a tax is imposed by section 55, under regulations proper adjustments shall be made for such year and all subsequent taxable years in the amounts taken into account under subparagraphs (A) and (B) of this paragraph and subparagraph (B) of subsection (d)(3).]

* * * * * * *

PART III—PROVISIONS OF GENERAL APPLICATION

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SEC. 847. SPECIAL ESTIMATED TAX PAYMENTS.

In the case of taxable years beginning after December 31, 1987, of an insurance company required to discount unpaid losses (as defined in section 846)—

(1) * * *

* * * * * * *

(9) Effect on earnings and profits. In determining the earnings and profits—

(A) * * *

* * * * * * *

[Nothing in the preceding sentence shall be construed to affect the application of section 56(g) (relating to adjustments based on adjusted current earnings).]

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

(A) providing for the separate application of this section with respect to each accident year, *and*

[(B) such adjustments in the application of this section as may be necessary to take into account the tax imposed by section 55, and]

[(C)] *(B)* providing for the application of this section in cases where the deduction allowed under paragraph (1) for any taxable year is less than the excess referred to in paragraph (1) for such year.

SEC. 848. CAPITALIZATION OF CERTAIN POLICY ACQUISITION EXPENSES.

(a) * * *

* * * * * * *

[(i) TREATMENT OF QUALIFIED FOREIGN CONTRACTS UNDER ADJUSTED CURRENT EARNINGS PREFERENCE.—For purposes of determining adjusted current earnings under section 56(g), acquisition expenses with respect to contracts described in clause (iii) of subsection (e)(1)(B) shall be capitalized and amortized in accordance with the treatment generally required under generally accepted accounting principles as if this subsection applied to such contracts for all taxable years.]

[(j)] *(i)* TRANSITIONAL RULE.—In the case of any taxable year which includes September 30, 1990, the amount taken into account as the net premiums (or negative capitalization amount) with respect to any category of specified insurance contracts shall be the amount which bears the same ratio to the amount which (but for this subsection) would be so taken into account as the number of days in such taxable year on or after September 30, 1990, bears to the total number of days in such taxable year.

* * * * * * *

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

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Subpart B—Foreign Corporations

* * * * * * *

SEC. 882. TAX ON INCOME OF FOREIGN CORPORATIONS CONNECTED WITH UNITED STATES BUSINESS.

(a) IMPOSITION OF TAX.—

(1) IN GENERAL.—A foreign corporation engaged in trade or business within the United States during the taxable year shall be taxable as provided in section 11, [55, 59A,] or 1201(a) on its taxable income which is effectively connected with the conduct of a trade or business within the United States.

* * * * * * *

PART III—INCOME FROM SOURCES WITHOUT THE UNITED STATES

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Subpart A—Foreign Tax Credit

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SEC. 904. LIMITATION ON CREDIT.

(a) * * *

* * * * * * *

(h) COORDINATION WITH NONREFUNDABLE PERSONAL CREDITS.—In the case of an individual, for purposes of subsection (a), the tax against which the credit is taken is such tax reduced by the sum of the credits allowable under subpart A of part IV of subchapter A of this chapter. This subsection shall not apply to taxable years beginning [during 2000 or 2001] *during 2000, 2001, 2002, or 2003*.

* * * * * * *

Subpart D—Possessions of the United States

* * * * * * *

SEC. 936. PUERTO RICO AND POSSESSION TAX CREDIT.

(a) ALLOWANCE OF CREDIT.—

(1) * * *

* * * * * * *

(3) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by paragraph (1) shall not be allowed against the tax imposed by—

[(A) section 59A (relating to environmental tax),]

[(B)] *(A)* section 531 (relating to the tax on accumulated earnings),

[(C)] *(B)* section 541 (relating to personal holding company tax), or

[(D)] *(C)* section 1351 (relating to recoveries of foreign expropriation losses).

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Subpart F—Controlled Foreign Corporations

* * * * * * *

SEC. 953. INSURANCE INCOME.

(a) * * *

* * * * * * *

(e) EXEMPT INSURANCE INCOME.—For purposes of this section—

(1) * * *

* * * * * * *

(10) APPLICATION.—This subsection and section 954(i) shall apply only to taxable years of a foreign corporation beginning after December 31, 1998[, and before January 1, 2002,] and to taxable years of United States shareholders with or within which any such taxable year of such foreign corporation ends. [If this subsection does not apply to a taxable year of a foreign corporation beginning after December 31, 2001 (and taxable years of United States shareholders ending with or within such taxable year), then, notwithstanding the preceding sentence, subsection (a) shall be applied to such taxable years in the same manner as it would if the taxable year of the foreign corporation began in 1998.]

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SEC. 954. FOREIGN BASE COMPANY INCOME.

(a) * * *

* * * * * * *

(h) SPECIAL RULE FOR INCOME DERIVED IN THE ACTIVE CONDUCT OF BANKING, FINANCING, OR SIMILAR BUSINESSES.—For purposes of subsection (c)(1), foreign personal holding company income shall not include qualified banking or financing income of an eligible controlled foreign corporation.

(2) * * *

* * * * * * *

(9) APPLICATION.—This subsection, subsection (c)(2)(C)(ii), and the last sentence of subsection (e)(2) shall apply only to taxable years of a foreign corporation beginning after December 31, 1998[, and before January 1, 2002,] and to taxable years of United States shareholders with or within which any such taxable year of such foreign corporation ends.

(i) SPECIAL RULE FOR INCOME DERIVED IN THE ACTIVE CONDUCT OF INSURANCE BUSINESS.—

(1) * * *

* * * * * * *

(4) METHODS FOR DETERMINING UNEARNED PREMIUMS AND RESERVES.—For purposes of paragraph (2)(A)—

(A) * * *

[(B) LIFE INSURANCE AND ANNUITY CONTRACTS.—The amount of the reserve of a qualifying insurance company or qualifying insurance company branch for any life insurance or annuity contract shall be equal to the greater of—

[(i) the net surrender value of such contract (as defined in section 807(e)(1)(A)), or

[(ii) the reserve determined under paragraph (5).]

(B) LIFE INSURANCE AND ANNUITY CONTRACTS.—

(i) IN GENERAL.—Except as provided in clause (ii), the amount of the reserve of a qualifying insurance company or qualifying insurance company branch for any life insurance or annuity contract shall be equal to the greater of—

(I) the net surrender value of such contract (as defined in section 807(e)(1)(A)), or

(II) the reserve determined under paragraph (5).

(ii) RULING REQUEST.—The amount of the reserve under clause (i) shall be the foreign statement reserve for the contract (less any catastrophe, deficiency, equalization, or similar reserves), if, pursuant to a ruling request submitted by the taxpayer, the Secretary determines that the factors taken into account in determining the foreign statement reserve provide an appropriate means of measuring income.

* * * * * * *

SEC. 962. ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX AT CORPORATE RATES.

(a) GENERAL RULE.—Under regulations prescribed by the Secretary, in the case of a United States shareholder who is an individual and who elects to have the provisions of this section apply for the taxable year—

(1) the tax imposed under this chapter on amounts which are included in his gross income under section 951(a) shall (in lieu of the tax determined under sections 1 and 55) be an amount equal to the tax which would be imposed under [sections 11 and 55] *section 11* if such amounts were received by a domestic corporation, and

* * * * * * *

Subchapter O—Gain or Loss on Disposition of Property

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PART II—BASIS RULES OF GENERAL APPLICATION

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SEC. 1016. ADJUSTMENTS TO BASIS.

(a) GENERAL RULE.—Proper adjustment in respect of the property shall in all cases be made—

(1) * * *

* * * * * * *

(20) for amounts allowed as deductions under section [59(e)] *59(d)* (relating to optional 10-year write-off of certain tax preferences);

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Subchapter P—Capital Gains and Losses

* * * * * * *

PART II—TREATMENT OF CAPITAL LOSSES

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SEC. 1211. LIMITATION ON CAPITAL LOSSES.

(a) * * *

(b) OTHER TAXPAYERS.—In the case of a taxpayer other than a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of the gains from such sales or exchanges, plus (if such losses exceed such gains) the lower of—

(1) * * *

* * * * * * *

Paragraph (1) shall be applied by substituting "$4,000" for "$3,000" and "$2,000" for "$1,500" in the case of taxable years beginning in 2001, and by substituting "$5,000" for "$3,000" and "$2,500" for "$1,500" in the case of taxable years beginning in 2002.

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Subchapter U—Designation and Treatment of Empowerment Zones, Enterprise Communities, and Rural Development Investment Areas

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PART IV—INCENTIVES FOR EDUCATION ZONES

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SEC. 1397E. CREDIT TO HOLDERS OF QUALIFIED ZONE ACADEMY BONDS.

(a) * * *

* * * * * * *

(e) LIMITATION ON AMOUNT OF BONDS DESIGNATED.—

(1) NATIONAL LIMITATION.—There is a national zone academy bond limitation for each calendar year. Such limitation is $400,000,000 for 1998, 1999, [2000, and 2001] *2000, 2001, 2002, and 2003*, and, except as provided in paragraph (4), zero thereafter.

* * * * * * *

CHAPTER 3—WITHHOLDING OF TAX ON NONRESIDENT ALIENS AND FOREIGN CORPORATIONS

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Subchapter A—Nonresident Aliens and Foreign Corporations

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SEC. 1445. WITHHOLDING OF TAX ON DISPOSITIONS OF UNITED STATES REAL PROPERTY INTERESTS.

(a) * * *

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(e) SPECIAL RULES RELATING TO DISTRIBUTIONS, ETC., BY CORPORATIONS, PARTNERSHIPS, TRUSTS, OR ESTATES.—

(1) CERTAIN DOMESTIC PARTNERSHIPS, TRUSTS, AND ESTATES.—In the case of any disposition of a United States real property interest as defined in section 897(c) (other than a disposition described in paragraph (4) or (5)) by a domestic partnership, domestic trust, or domestic estate, such partnership, the trustee of such trust, or the executor of such estate (as the case may be) shall be required to deduct and withhold under subsection (a) a tax equal to 35 percent (or, to the extent provided in regulations, [20] *18* percent) of the gain realized to the extent such gain—

(A) * * *

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CHAPTER 6—CONSOLIDATED RETURNS

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Subchapter B—Related Rules

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PART II—CERTAIN CONTROLLED CORPORATIONS

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SEC. 1561. LIMITATIONS ON CERTAIN MULTIPLE TAX BENEFITS IN THE CASE OF CERTAIN CONTROLLED CORPORATIONS.

(a) GENERAL RULE.—The component members of a controlled group of corporations on a December 31 shall, for their taxable

years which include such December 31, be limited for purposes of this subtitle to—

(1) * * *

(2) one $250,000 ($150,000 if any component member is a corporation described in section 535(c)(2)(B) amount for purposes of computing the accumulated earnings credit under section 535(c)(2) and (3), *and*

(3) one $40,000 exemption amount for purposes of computing the amount of the minimum tax**[**, and**]**.

[(4) one $2,000,000 amount for purposes of computing the tax imposed by section 59A.**]**

The amounts specified in paragraph (1), the amount specified in paragraph (3), and the amount specified in paragraph (4) shall be divided equally among the component members of such group on such December 31 unless all of such component members consent (at such time and in such manner as the Secretary shall by regulations prescribe) to an apportionment plan providing for an unequal allocation of such amounts. The amounts specified in paragraph (2) shall be divided equally among the component members of such group on such December 31 unless the Secretary prescribes regulations permitting an unequal allocation of such amounts. Notwithstanding paragraph (1), in applying the last 2 sentences of section 11(b)(1) to such component members, the taxable income of all such component members shall be taken into account and any increase in tax under such last sentence shall be divided among such component members in the same manner as amounts under paragraph (1). **[**In applying section 55(d)(3), the alternative minimum taxable income of all component members shall be taken into account and any decrease in the exemption amount shall be allocated to the component members in the same manner as under paragraph (3).**]**

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Subtitle C—Employment Taxes

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CHAPTER 23—FEDERAL UNEMPLOYMENT TAX ACT

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SEC. 3304. APPROVAL OF STATE LAWS.

(a) REQUIREMENTS.—The Secretary of Labor shall approve any State law submitted to him, within 30 days of such submission, which he finds provides that—

(1) * * *

* * * * * * *

(4) all money withdrawn from the unemployment fund of the State shall be used solely in the payment of unemployment compensation, exclusive of expenses of administration, and for refunds of sums erroneously paid into such fund and refunds paid in accordance with the provisions of section 3305(b); except that—

(A) * * *

(B) the amounts specified by section 903(c)(2) *or 903(d)(4)* of the Social Security Act may, subject to the conditions prescribed in such section, be used for expenses incurred by the State for administration of its unemployment compensation law and public employment offices;

* * * * * * *

SEC. 3306. DEFINITIONS.

(a) * * *

* * * * * * *

(f) UNEMPLOYMENT FUND.—For purposes of this chapter, the term "unemployment fund" means a special fund, established under a State law and administered by a State agency, for the payment of compensation. Any sums standing to the account of the State agency in the Unemployment Trust Fund established by section 904 of the Social Security Act, as amended (42 U.S.C. 1104), shall be deemed to be a part of the unemployment fund of the State, and no sums paid out of the Unemployment Trust Fund to such State agency shall cease to be a part of the unemployment fund of the State until expended by such State agency. An unemployment fund shall be deemed to be maintained during a taxable year only if throughout such year, or such portion of the year as the unemployment fund was in existence, no part of the moneys of such fund was expended for any purpose other than the payment of compensation (exclusive of expenses of administration) and for refunds of sums erroneously paid into such fund and refunds paid in accordance with the provisions of section 3305(b); except that—

(1) * * *

(2) the amounts specified by section 903(c)(2) *or 903(d)(4)* of the Social Security Act may, subject to the conditions prescribed in such section, be used for expenses incurred by the State for administration of its unemployment compensation law and public employment offices;

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Subtitle F—Procedure and Administration

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CHAPTER 65—ABATEMENTS, CREDITS, AND REFUNDS

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Subchapter B—Rules for Special Application

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SEC. 6425. ADJUSTMENT OF OVERPAYMENT OF ESTIMATED INCOME TAX BY CORPORATION.

(a) * * *

* * * * * * *

(c) DEFINITIONS.—For purposes of this section and section 6655(h) (relating to excessive adjustment)—

(1) The term "income tax liability" means the excess of—

[(A) The sum of—

[(i) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever is applicable,

[(ii) the tax imposed by section 55, plus

[(iii) the tax imposed by section 59A, over]

(A) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever is applicable, over

* * * * * * *

SEC. 6428. ACCELERATION OF 10 PERCENT INCOME TAX RATE BRACKET BENEFIT FOR 2001.

(a) * * *

* * * * * * *

(d) SPECIAL RULES.—

(1) COORDINATION WITH ADVANCE REFUNDS OF CREDIT.—

(A) IN GENERAL.—The amount of credit which would (but for this paragraph) be allowable under this section shall be reduced (but not below zero) by the aggregate refunds and credits made or allowed to the taxpayer under [subsection (e)] *subsections (e) and (f)*. Any failure to so reduce the credit shall be treated as arising out of a mathematical or clerical error and assessed according to section 6213(b)(1).

(B) JOINT RETURNS.—In the case of a refund or credit made or allowed under [subsection (e)] *subsection (e) or (f)* with respect to a joint return, half of such refund or credit shall be treated as having been made or allowed to each individual filing such return.

* * * * * * *

(e) ADVANCE REFUNDS OF CREDIT BASED ON PRIOR YEAR DATA.—

(1) * * *

* * * * * * *

(3) TIMING OF PAYMENTS.—In the case of any overpayment attributable to this subsection, the Secretary shall, subject to the provisions of this title, refund or credit such overpayment as rapidly as possible and, to the extent practicable, before October 1, 2001. No refund or credit shall be made or allowed under this subsection after [December 31, 2001] *the date of the enactment of the Economic Security and Recovery Act of 2001*.

* * * * * * *

(f) SUPPLEMENTAL REBATE.—

(1) IN GENERAL.—Each individual who was an eligible individual for such individual's first taxable year beginning in 2000 and who, before October 16, 2001, filed a return of tax imposed by subtitle A for such taxable year shall be treated as having made a payment against the tax imposed by chapter 1 for such first taxable year in an amount equal to the supplemental refund amount for such taxable year.

(2) SUPPLEMENTAL REFUND AMOUNT.—For purposes of this subsection, the supplemental refund amount is an amount equal to the excess (if any) of—

(A)(i) $600 in the case of taxpayers to whom section 1(a) applies,

(ii) $500 in the case of taxpayers to whom section 1(b) applies, and

(iii) $300 in the case of taxpayers to whom subsections (c) or (d) of section 1 applies, over

(B) the taxpayer's advance refund amount under subsection (e).

(3) TIMING OF PAYMENTS.—In the case of any overpayment attributable to this subsection, the Secretary shall, subject to the provisions of this title, refund or credit such overpayment as rapidly as possible.

(4) NO INTEREST.—No interest shall be allowed on any overpayment attributable to this subsection.

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CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, AND ASSESSABLE PENALTIES

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Subchapter A—Additions to the Tax, Additional Amounts

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PART I—GENERAL PROVISIONS

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SEC. 6655. FAILURE BY CORPORATION TO PAY ESTIMATED INCOME TAX.

(a) * * *

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(e) LOWER REQUIRED INSTALLMENT WHERE ANNUALIZED INCOME INSTALLMENT OR ADJUSTED SEASONAL INSTALLMENT IS LESS THAN AMOUNT DETERMINED UNDER SUBSECTION (D).—

(1) * * *

(2) DETERMINATION OF ANNUALIZED INCOME INSTALLMENT.—

(A) IN GENERAL.—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 modified alternative minimum taxable income**]**—

(I) for the first 3 months of the taxable year, in the case of the 1st required installment,

(II) for the first 3 months of the taxable year, in the case of the 2nd required installment,

(III) for the first 6 months of the taxable year in the case of the 3rd required installment, and

(IV) for the first 9 months of the taxable year, in the case of the 4th required installment, over

(ii) the aggregate amount of any prior required installments for the taxable year.

(B) SPECIAL RULES.—For purposes of this paragraph—

(i) ANNUALIZATION.—The taxable income[, alternative minimum taxable income, and modified alternative minimum taxable income] shall be placed on an annualized basis under regulations prescribed by the Secretary.

* * * * * * *

[(iii) MODIFIED ALTERNATIVE MINIMUM TAXABLE INCOME.—The term "modified alternative minimum taxable income" has the meaning given to such term by section 59A(b).]

* * * * * * *

(g) DEFINITIONS AND SPECIAL RULES.—

(1) TAX.—For purposes of this section, the term "tax" means the excess of—

[(A) the sum of—

[(i) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever applies,

[(ii) the tax imposed by section 55,

[(iii) the tax imposed by section 59A, plus

[(iv) the tax imposed by section 887, over]

(A) the sum of—

(i) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever applies, plus

(ii) the tax imposed by section 887, over

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CHAPTER 77—MISCELLANEOUS PROVISIONS

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SEC. 7518. TAX INCENTIVES RELATING TO MERCHANT MARINE CAPITAL CONSTRUCTION FUNDS.

(a) * * *

* * * * * * *

(g) TAX TREATMENT OF NONQUALIFIED WITHDRAWALS.—

(1) * * *

* * * * * * *

(6) NONQUALIFIED WITHDRAWALS TAXED AT HIGHEST MARGINAL RATE.—

(A) IN GENERAL.—In the case of any taxable year for which there is a nonqualified withdrawal (including any amount so treated under paragraph (5)), the tax imposed by chapter 1 shall be determined—

(i) * * *

* * * * * * *

With respect to the portion of any nonqualified withdrawal made out of the capital gain account during a taxable year to which section 1(h) or 1201(a) applies, the rate of tax taken into account under the preceding sentence shall not exceed [20] *18* percent (34 percent in the case of a corporation).

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CHAPTER 78—DISCOVERY OF LIABILITY AND ENFORCEMENT OF TITLE

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Subchapter D—Possessions

* * * * * * *

SEC. 7652. SHIPMENTS TO THE UNITED STATES.

(a) * * *

* * * * * * *

(f) LIMITATION ON COVER OVER OF TAX ON DISTILLED SPIRITS.—For purposes of this section, with respect to taxes imposed under section 5001 or this section on distilled spirits, the amount covered into the treasuries of Puerto Rico and the Virgin Islands shall not exceed the lesser of the rate of—

(1) $10.50 ($13.25 in the case of distilled spirits brought into the United States after June 30, 1999, and before January 1, [2002] *2004*), or

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Subtitle K—Group Health Plan Requirements

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CHAPTER 100—GROUP HEALTH PLAN REQUIREMENTS

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Subchapter B—Other Requirements

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SEC. 9812. PARITY IN THE APPLICATION OF CERTAIN LIMITS TO MENTAL HEALTH BENEFITS.

(a) * * *

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(f) SUNSET.—This section shall no apply to benefits for services furnish on or after September 30, [2001] *2003*.

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SECTION 607 OF THE MERCHANT MARINE ACT, 1936

SEC. 607. (a) * * *

* * * * * * *

(h) Tax Treatment of Nonqualified Withdrawals.

(1) * * *

* * * * * * *

(6) NONQUALIFIED WITHDRAWALS TAXED AT HIGHEST MARGINAL RATE.—

(A) IN GENERAL.—In the case of any taxable year for which there is a nonqualified withdrawal (including any amount so treated under paragraph (5)), the tax imposed by chapter 1 of the Internal Revenue Code of 1986 shall be determined—

(i) * * *

* * * * * * *

With respect to the portion of any nonqualified withdrawal made out of the capital gain account during a taxable year to which section l(h) or 1201(a) of such Code applies, the rate of tax taken into account under the preceding sentence shall not exceed [20] *18* percent (34 percent in the case of a corporation).

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TAXPAYER RELIEF ACT OF 1997

* * * * * * *

TITLE III—SAVINGS AND INVESTMENT INCENTIVES

* * * * * * *

Subtitle B—Capital Gains

SEC. 311. MAXIMUM CAPITAL GAINS RATES FOR INDIVIDUALS.

(a) * * *

* * * * * * *

[(e) ELECTION TO RECOGNIZE GAIN ON ASSETS HELD ON JANUARY 1, 2001.—For purposes of the Internal Revenue Code of 1986—

[(1) IN GENERAL.—A taxpayer other than a corporation may elect to treat—

[(A) any readily tradable stock (which is a capital asset) held by such taxpayer on January 1, 2001, and not sold before the next business day after such date, as having been sold on such next business day for an amount equal to its closing market price on such next business day (and as having been reacquired on such next business day for an amount equal to such closing market price), and

[(B) any other capital asset or property used in the trade or business (as defined in section 1231(b) of the In-

ternal Revenue Code of 1986) held by the taxpayer on January 1, 2001, as having been sold on such date for an amount equal to its fair market value on such date (and as having been reacquired on such date for an amount equal to such fair market value).

[(2) TREATMENT OF GAIN OR LOSS.—

[(A) Any gain resulting from an election under paragraph (1) shall be treated as received or accrued on the date the asset is treated as sold under paragraph (1) and shall be recognized notwithstanding any provision of the Internal Revenue Code of 1986.

[(B) Any loss resulting from an election under paragraph (1) shall not be allowed for any taxable year.

[(3) ELECTION.—An election under paragraph (1) shall be made in such manner as the Secretary of the Treasury or his delegate may prescribe and shall specify the assets for which such election is made. Such an election, once made with respect to any asset, shall be irrevocable. Such an election shall not apply to any asset which is disposed of (in a transaction in which gain or loss is recognized in whole or in part) before the close of the 1-year period beginning on the date that the asset would have been treated as sold under such election.

[(4) READILY TRADABLE STOCK.—For purposes of this subsection, the term "readily tradable stock" means any stock which, as of January 1, 2001, is readily tradable on an established securities market or otherwise.]

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TITLE IX—MISCELLANEOUS PROVISIONS

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Subtitle G—Other Provisions

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SEC. 971. EXEMPTION OF THE INCREMENTAL COST OF A CLEAN FUEL VEHICLE FROM THE LIMITS ON DEPRECIATION FOR VEHICLES.

(a) * * *

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(b) EFFECTIVE DATE.—The amendments made by this section shall apply to property placed in service after the date of enactment of this Act [and before January 1, 2005].

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TITLE X—REVENUES

* * * * * * *

Subtitle D—Excise and Employment Tax Provisions

* * * * * * *

SEC. 1032. KEROSENE TAXED AS DIESEL FUEL.

(a) * * *

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(f) EFFECTIVE DATES.—

(1) Except as provided in paragraph (2), the amendments made by this section shall take effect on July 1, 1998.

(2) The amendment made by subsection (d) shall take effect on January 1, **[**2002**]** *2004*.

* * * * * * *

SOCIAL SECURITY ACT

* * * * * * *

TITLE III—GRANTS TO STATES FOR UNEMPLOYMENT COMPENSATION ADMINISTRATION

* * * * * * *

PROVISIONS OF STATE LAWS

SEC. 303. (a) The Secretary of Labor shall make no certification for payment to any State unless he finds that the law of such State, approved by the Secretary of Labor under the Federal Unemployment Tax Act, includes provision for—

(1) * * *

* * * * * * *

(5) Expenditure of all money withdrawn from an unemployment fund of such State, in the payment of unemployment compensation, exclusive of expenses of administration, and for refunds of sums erroneously paid into such fund and refunds paid in accordance with the provisions of 3305(b) of the Federal Unemployment Tax Act: *Provided,* That an amount equal to the amount of employee payments in to the unemployment fund of a State may be used in the payment of cash benefits to individuals with respect to their disability, exclusive of expenses of administration: *Provided further,* That the amounts specified by section 903(c)(2) *or 903(d)(4)* may, subject to the conditions prescribed in such section, be used for expenses incurred by the State for administration of its unemployment compensation law and public employment offices: *Provided further,* That nothing in this paragraph shall be construed to prohibit deducting an amount from unemployment compensation otherwise payable to an individual and using the amount so deducted to pay for health insurance, or the withholding of Federal, State, or local individual income tax, if the individual elected to have such deduction made and such deduction was made under a program approved by the Secretary of Labor: *Provided further,* That amounts may be deducted from unem-

ployment benefits and used to repay overpayments as provided in subsection (g): *Provided further,* That amounts may be withdrawn for the payment of short-time compensation under a plan approved by the Secretary of Labor: *Provided further,* That amounts may be withdrawn for the payment of allowances under a self-employment assistance program (as defined in section 3306(t) of the Internal Revenue Code of 1986); and

* * * * * * *

TITLE IX—MISCELLANEOUS PROVISIONS RELATING TO EMPLOYMENT SECURITY

* * * * * * *

AMOUNTS TRANSFERRED TO STATE ACCOUNTS

In General

SEC. 903. (a)(1) * * *

* * * * * * *

[(3)(A) Notwithstanding any other provision of this section, for purposes of carrying out this subsection with respect to any excess amount (referred to in paragraph (1)) remaining in the employment security administration account as of the close of fiscal year 1999, 2000, or 2001, such amount shall—

[(i) to the extent of any amounts not in excess of $100,000,000, be subject to subparagraph (B), and

[(ii) to the extent of any amounts in excess of $100,000,000, be subject to subparagraph (C).

[(B) Paragraphs (1) and (2) shall apply with respect to any amounts described in subparagraph (A)(i), except that—

[(i) in carrying out the provisions of paragraph (2)(B) with respect to such amounts (to determine the portion of such amounts which is to be allocated to a State for a succeeding fiscal year), the ratio to be applied under such provisions shall be the same as the ratio that—

[(I) the amount of funds to be allocated to such State for such fiscal year pursuant to the base allocation formula under title III, bears to

[(II) the total amount of funds to be allocated to all States for such fiscal year pursuant to the base allocation formula under title III,

as determined by the Secretary of Labor, and

[(ii) the amounts allocated to a State pursuant to this subparagraph shall be available to such State, subject to the last sentence of subsection (c)(2).

Nothing in this paragraph shall preclude the application of subsection (b) with respect to any allocation determined under this subparagraph.

[(C) Any amounts described in clause (ii) of subparagraph (A) (remaining in the employment security administration account as of the close of any fiscal year specified in such subparagraph) shall, as of the beginning of the succeeding fiscal year, accrue to the Fed-

eral unemployment account, without regard to the limit provided in section 902(a).]

* * * * * * *

Use of Transferred Amounts

(c)(1) * * *

(2) A State may, pursuant to a specific appropriation made by the legislative body of the State, use money withdrawn from its account in the payment of expenses incurred by it for the administration of its unemployment compensation law and public employment offices if and only if—

(A) * * *

* * * * * * *

[Any amount allocated to a State under this section for fiscal year 2000, 2001, or 2002 may be used by such State only to pay expenses incurred by it for the administration of its unemployment compensation law, and may be so used by it without regard to any of the conditions prescribed in any of the preceding provisions of this paragraph.]

* * * * * * *

Special Transfer in Fiscal Year 2002

(d)(1) The Secretary of the Treasury shall transfer (as of the date determined under paragraph (5)(A)) from the Federal unemployment account to the account of each State in the Unemployment Trust Fund the amount determined with respect to such State under paragraph (2).

(2) The amount to be transferred under this subsection to a State account shall (as determined by the Secretary of Labor and certified by such Secretary to the Secretary of the Treasury) be equal to—

(A) the amount which would have been required to have been transferred under this section to such account at the beginning of fiscal year 2002 if section 402(a)(1) of the Economic Security and Recovery Act of 2001 had been enacted before the close of fiscal year 2001, minus

(B) the amount which was in fact transferred under this section to such account at the beginning of fiscal year 2002.

(3)(A) Except as provided in paragraph (4), amounts transferred to a State account pursuant to this subsection may be used only in the payment of cash benefits—

(i) to individuals with respect to their unemployment, and

(ii) which are allowable under subparagraph (B) or (C).

(B)(i) At the option of the State, cash benefits under this paragraph may include amounts which shall be payable as regular or additional compensation for individuals eligible for regular compensation under the unemployment compensation law of such State.

(ii) Any additional compensation under clause (i) may not be taken into account for purposes of any determination relating to the amount of any extended compensation for which an individual might be eligible.

(C)(i) At the option of the State, cash benefits under this paragraph may include amounts which shall be payable to 1 or more

categories of individuals not otherwise eligible for regular compensation under the unemployment compensation law of such State.

(ii) The benefits paid under this subparagraph to any individual may not, for any period of unemployment, exceed the maximum amount of regular compensation authorized under the unemployment compensation law of such State for that same period, plus any additional benefits (described in subparagraph (B)(i)) which could have been paid with respect to that amount.

(D) Amounts transferred to a State account under this subsection may be used in the payment of cash benefits to individuals only for weeks of unemployment—

(i) beginning after the date of enactment of this subsection, and

(ii) ending on or before March 11, 2003.

(4) Amounts transferred to a State account under this subsection may be used for the administration of its unemployment compensation law and public employment offices (including in connection with benefits described in paragraph (3) and any recipients thereof), subject to the same conditions as set forth in subsection (c)(2) (excluding subparagraph (B) thereof, and deeming the reference to "subsections (a) and (b)" in subparagraph (D) thereof to include this subsection).

(5) Transfers under this subsection—

(A) shall be made on such date as the Secretary of Labor (in consultation with the Secretary of the Treasury) shall determine, but in no event later than 10 days after the date of enactment of this subsection, and

(B) may, notwithstanding any other provision of this subsection, be made only to the extent that they do not to exceed—

(i) the balance in the Federal unemployment account as of the date determined under subparagraph (A), or

(ii) the total amount that was transferred under this section to the Federal unemployment account at the beginning of fiscal year 2002,

whichever is less.

* * * * * * *

TITLE XX—BLOCK GRANTS TO STATES FOR SOCIAL SERVICES

* * * * * * *

SEC. 2008. GRANTS FOR HEALTH CARE ASSISTANCE FOR THE UNEMPLOYED.

(a) FUNDING.—For purposes of section 2003, the amount specified in section 2003(c) for fiscal year 2002 is increased by $3,000,000,000.

(b) USE OF FUNDS.—Notwithstanding any other provision of this title, to the extent that an amount paid to a State under section 2002 is attributable to funds made available by reason of subsection (a) of this section—

(1) the State shall use the amount to assist an unemployed individual who is not eligible for Federal health coverage to purchase health care coverage for the individual or any member of the family of the individual who is not so eligible; and

(2) the amount—

(A) shall be used to supplement, not supplant, any other Federal, State, or local funds that are used for the provision of health care coverage; and

(B) may not be included in determining the amount of non-Federal contributions required under any program.

(c) DEFINITIONS.—In this section:

(1) UNEMPLOYED INDIVIDUAL.—The term "unemployed individual" means an individual who—

(A) is without a job (determined in accordance with the criteria used by the Bureau of Labor Statistics of the Department of Labor in defining individuals as unemployed);

(B) is seeking and available for work; and

(C) has or had a benefit year (within the meaning of section 205 of the Federal-State Extended Unemployment Compensation Act of 1970) beginning on or after January 1, 2001.

(2) FEDERAL HEALTH COVERAGE.—

(A) IN GENERAL.—Subject to subparagraph (B), the term "Federal health coverage" means coverage under any medical care program described in—

(i) title XVIII, XIX, or XXI of this Act (other than under section 1928);

(ii) chapter 55 of title 10, United States Code;

(iii) chapter 17 of title 38, United States Code;

(iv) chapter 89 of title 5, United States Code (other than coverage which is comparable to continuation coverage under section 4980B of the Internal Revenue Code of 1986); or

(v) the Indian Health Care Improvement Act.

(B) SPECIAL RULE.—Such term does not include coverage under a qualified long-term care insurance contract.

* * * * * * *

VII. DISSENTING VIEWS

Democrats support a balanced, fiscally-responsible economic recovery package. It should provide vital relief for laid-off workers and temporary tax cuts for businesses and individuals that will directly stimulate the economy. It should leave room for essential security priorities. It should not hurt our ability to restore Social Security and Medicare surpluses and rebuild long-term confidence in our economy.

A bipartisan stimulus package should help those people in need because of the economic downturn. Hundreds of thousands of Americans have lost their jobs in recent weeks and, as a result, many lack health insurance and unemployment benefits. They are worried about basic needs like paying the rent and feeding their families. They care about both their personal and their economic security.

The American people are depending on Members of Congress to cooperate and work with each other. They should expect and get no less. While we are fighting a war against terrorism, we can not afford to fight a political war against each other.

The Democrats will continue, in every possible way, to cooperate with our Republican friends. There already have been some post-September 11th bipartisan agreements, such as the Cardin-Houghton Unemployment Insurance bill. In contrast, Committee Chairman Thomas has spurned attempts at bipartisan cooperation in developing an economic stimulus bill. The Committee bill neither addresses the priorities of the House and Senate Democrats, House and Senate Republicans, or the President, based on his comments. Chairman Thomas has forced a partisan debate by preparing unilaterally his own version of an economic stimulus package (one that both the Committee Democrats and Committee Republicans did not see until shortly before the markup.)

We are very concerned that the Committee bill violates the bipartisan principles for economic stimulus signed by the House and Senate budget committee Chairmen and Ranking Members and supported by many Members of both Congressional bodies. This was the basis of our ongoing bipartisan discussions and guidance for how we would act quickly to develop the economic stimulus package for which all Americans are waiting. That agreement stipulates that the stimulus package should be temporary and have immediate, short-term stimulus impact; be directly related to economic stimulus and relief; and be disciplined in size and paid for over time through offsets. The Committee bill does not fulfill these important bipartisan principles. As a result, the Committee's bill does not provide for an effective economic stimulus package which we can all support.

The Committee bill is not temporary. The provisions do not provide "economic stimulus" along the lines recommended by Federal

Reserve Chairman Greenspan. Instead of temporary tax cuts, many of the Committee tax provisions are permanent and provide little or nothing in terms of stimulus within the next 15 months. Further, the Committee bill will not help rebuild long-term confidence in the economy. It creates new budgetary pressures which will threaten efforts to strengthen Social Security and Medicare, pay down debt, and restore economic confidence.

The Committee bill is not directly related to economic stimulus and relief. The proposal's tax cuts do not maximize consumer demand by focusing on those low- and middle-income households most likely to spend the money. The lion's share of individual tax cuts in the Committee bill goes to the wealthy, and many of the business tax cuts go to businesses that are least in need of relief. The Committee bill includes permanent tax cuts that have nothing to do with the terrorist attack or its economic aftermath. Rather, the bill provides special interests with tax cuts they have wanted for years.

The Committee bill will cost nearly $160 billion over the next ten years and is not paid for through offsets. The bill ignores the need for out-year offsets to make up over time for the cost of near-term economic stimulus. This is not fiscally responsible. Our economic stimulus package should be focused and be paid for through short- and long-term revenue offsets.

There are provisions about which the Democrats feel very strongly. An economic stimulus package must include measures that benefits all Americans in need. Among them are proposals to address our Nation's security concerns, to expand unemployment insurance benefits, and to make health insurance available to those who have lost their jobs.

The Committee bill does not allow us to address Americans' security concerns. The bill puts tax cuts first. Such an approach does not leave room for vital improvements in the security of airports, seaports, dams, power plants, public buildings, roads, railroads, bridges and tunnels throughout the country. The American public has spoken loudly and clearly that its priority is to significantly increase security in the U.S. and to protect American families.

The Committee bill fails to guarantee any unemployed worker increased or extended unemployment compensation. In fact, the bill's special Reed Act transfer of funding to the states ensures that almost no action will occur over the next six months to help jobless Americans because state legislatures will take at least that long to meet and decide how to allocate the funding. Additionally, there is nothing in the legislation that would prevent states from using the Reed Act money to replace state funding for unemployment benefits—meaning the net result could be no new assistance for displaced workers.

The Committee bill does not protect newly unemployed individuals and their families and other affected by the terrorist attacks from the very real danger that they will lose their health insurance and join the ranks of the nearly 40 million uninsured Americans. Many unemployed are eligible to stay on their former employers' insurance plans, but at a cost of 102 percent of the premium. (In 2002, this is projected to average $600 per month, or $7,200 per year.) Unfortunately, few can afford to maintain this coverage

under current law. The Committee bill fails to provide meaningful assistance with health insurance. Use of the Social Services Block Grant will needlessly delay distribution of funds, and the Committee allocation of $3 billion offers too little for too few.

The most effective and efficient manner by which to provide quick, short-term assistance with health insurance coverage is to build on existing programs, namely a subsidy for COBRA coverage for those who are eligible and a temporary expansion of Medicaid and CHIP for those who are not.

Importantly, the Committee bill is not bipartisan. This means the bill will not be enacted into law. There is no excuse for unilateral action by the Ways and Means Committee Chairman at a time when the House, the Senate, and the President are meeting on a bipartisan basis to hammer out a meaningful economic stimulus package. Unfortunately, the Committee bill may be effective in "stimulating increased campaign contributions," but not effective in "stimulating the economy."

The several bipartisan meetings held during the past weeks among the bicameral leaders of both tax-writing Committees and the Administration were very encouraging. It is unfortunate that the Committee Chairman decided to pull out and act before the bipartisan process was complete. However, it is not too late. Our House leaders, Democrats and Republicans, are committed to moving forward a bipartisan economic stimulus bill. We will continue to follow their lead.

We look forward to the development of an effective, bipartisan package to stimulate our economy and to address the needs of Americans after the horrific events of September 11, 2001. One thing is clear: the bipartisan bill will not be H.R. 3090. It does not address what Americans need and want.

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