

105TH CONGRESS
1ST SESSION

S. 673

To amend the Internal Revenue Code of 1986 and Employee Retirement Income Security Act of 1974 in order to promote and improve employee stock ownership plans.

IN THE SENATE OF THE UNITED STATES

APRIL 30, 1997

Mr. BREAUX (for himself and Mr. HATCH) introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 and Employee Retirement Income Security Act of 1974 in order to promote and improve employee stock ownership plans.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “ESOP Promotion Act
5 of 1997”.

1 **SEC. 2. PROVISIONS RELATING TO S CORPORATIONS ES-**
 2 **TABLISHING EMPLOYEE STOCK OWNERSHIP**
 3 **PLANS.**

4 (a) REPEAL OF PROVISION MAKING CERTAIN ESOP
 5 BENEFITS INAPPLICABLE TO S CORPORATIONS.—Section
 6 1316(d) of the Small Business Job Protection Act of 1996
 7 is repealed, and the Internal Revenue Code of 1986 shall
 8 be applied and administered as if the amendments made
 9 by such section had not been enacted.

10 (b) REPEAL OF APPLICATION OF UNRELATED BUSI-
 11 NESS INCOME TAX.—Section 512(e) of the Internal Reve-
 12 nue Code of 1986 is amended—

13 (1) by striking “described in section
 14 1361(c)(7)” in paragraph (1) and inserting “de-
 15 scribed in section 501(c)(3) and exempt from tax-
 16 ation under section 501(a)”, and

17 (2) by inserting “CHARITABLE ORGANIZATIONS
 18 HOLDING STOCK IN” after “APPLICABLE TO” in the
 19 heading.

20 (c) ESOPs ALLOWED TO DISTRIBUTE CASH RATH-
 21 ER THAN STOCK.—

22 (1) IN GENERAL.—Section 409(h)(2) of the In-
 23 ternal Revenue Code of 1986 is amended by adding
 24 at the end the following new subparagraph:

25 “(8) PLAN MAINTAINED BY S CORPORA-
 26 TION.—In the case of a plan established and

1 maintained by an S corporation which otherwise
2 meets the requirements of this subsection or
3 section 4975(e)(7), such plan shall not be treat-
4 ed as failing to meet the requirements of this
5 subsection or section 401(a) merely because it
6 does not permit a participant to exercise the
7 right described in paragraph (1)(A) if such plan
8 provides that the participant entitled to a dis-
9 tribution from the plan shall have a right to re-
10 ceive the distribution in cash.”

11 (2) CONFORMING AMENDMENTS.—Section
12 409(h)(2) of such Code is amended—

13 (A) by striking “A plan” and inserting:

14 “(A) IN GENERAL.—A plan”, and

15 (B) by striking “In the case of an em-
16 ployer” and inserting:

17 “(B) PLANS RESTRICTED BY CHARTER OR
18 BYLAWS.—In the case of an employer”.

19 (d) EXEMPTIONS FROM PROHIBITED TRANSACTION
20 RULES AVAILABLE TO ESOPs AND SHAREHOLDER EM-
21 PLOYEES.—The last sentence of section 408(d) of the Em-
22 ployee Retirement Income Security Act of 1974 (29
23 U.S.C. 1108(d)) is amended by striking all that precedes
24 “a participant or beneficiary” and inserting “For purposes
25 of this subsection,”.

1 (e) EFFECTIVE DATE.—The amendments made by
2 this section shall apply to taxable years beginning after
3 December 31, 1997.

4 **SEC. 3. AMENDMENTS RELATED TO SECTION 1042.**

5 (a) EXTENSION OF SECTION 1042 PRINCIPLES TO
6 STOCK RECEIVED AS COMPENSATION FOR SERVICES.—

7 (1) IN GENERAL.—Section 83 of the Internal
8 Revenue Code of 1986 (relating to property trans-
9 ferred in connection with performance of services) is
10 amended by adding at the end the following new
11 subsection:

12 “(i) EXCEPTION FOR TRANSFERS OF QUALIFIED SE-
13 CURITIES SOLD TO EMPLOYEE STOCK OWNERSHIP
14 PLANS.—

15 “(1) EXCLUSION FROM INCOME.—Subsections
16 (a) and (b) shall not apply to, and no amount shall
17 be includible in gross income with respect to, the
18 transfer of any qualified security (as defined in sec-
19 tion 1042(c)(1)) in connection with the performance
20 of services if, and to the extent that, within 60 days
21 after the event which would cause the recognition of
22 income pursuant to subsection (a) or (b) but for this
23 subsection, the transferee sells such qualified secu-
24 rity to an employee stock ownership plan (as defined

1 in section 4975(e)(7)) and the requirements of sec-
2 tion 1042(a) are met with respect to such sale.

3 “(2) NO DEDUCTION BY EMPLOYER.—Notwith-
4 standing the provisions of subsection (h), the person
5 for whom the services were performed in connection
6 with which any qualified security is transferred shall
7 not be entitled to a deduction with respect to such
8 transfer if, and to the extent that, paragraph (1) ap-
9 plies to such transfer.”

10 (2) CONFORMING AMENDMENTS.—

11 (A) Section 424(c)(1) of such Code is
12 amended by striking “or” at the end of sub-
13 paragraph (B), by striking the period at the
14 end of subparagraph (C) and inserting “, or”,
15 and by adding at the end the following new sub-
16 paragraph:

17 “(D) a sale to which section 1042 applies.”

18 (B) Section 1042(a) of such Code is
19 amended—

20 (i) by striking “which would be recog-
21 nized as long-term capital gain” from the
22 first sentence thereof, and

23 (ii) by adding at the end the following
24 new sentence: “Any gain which is recog-
25 nized after the application of the preceding

1 sentence shall be treated as ordinary in-
2 come to the extent of the lesser of the
3 amount of such gain or the amount which
4 would have been treated as ordinary in-
5 come but for this section.”

6 (C) Section 1042(b)(4) of such Code is
7 amended by adding at the end the following
8 new sentence: “The requirements of the preced-
9 ing sentence shall not apply to qualified securi-
10 ties received by the taxpayer in a transfer to
11 which section 83 or 422 applied (or to which
12 section 422 or 424 (as in effect on the day be-
13 fore the date of enactment of the Revenue Rec-
14 onciliation Act of 1990) applied).”

15 (D) Section 1042(c)(1)(B) of such Code is
16 amended to read as follows:

17 “(B) were not received by the taxpayer
18 in—

19 “(i) a distribution from a plan de-
20 scribed in section 401(a), or

21 “(ii) a transfer pursuant to a right to
22 acquire stock to which section 423 ap-
23 plied.”

24 (E) The first sentence of section 1042(d)
25 of such Code is amended to read as follows:

1 “The basis of the taxpayer in qualified replace-
2 ment property purchased by the taxpayer dur-
3 ing the replacement period shall be reduced by
4 the amount of gain not recognized by virtue of
5 such purchase, taking into account the applica-
6 tion of subsection (a) and, if applicable, the ap-
7 plication of section 83(i) or section
8 424(c)(1)(D).”

9 (F) Section 1042(e)(1) of such Code is
10 amended to read as follows:

11 “(1) IN GENERAL.—If a taxpayer disposes of
12 any qualified replacement property, then, notwith-
13 standing any other provision of this title, gain (if
14 any) shall be recognized to the extent of the gain
15 which was not recognized by reason of the acquisi-
16 tion by such taxpayer of such qualified replacement
17 property, taking into account the application of sub-
18 section (a) and, if applicable, the application of sec-
19 tion 83(i) or 424(c)(1)(D). Such gain shall be treat-
20 ed as ordinary income to the extent of the excess (if
21 any) of the amount which would have been treated
22 as ordinary income but for the application of such
23 sections over the amount treated as ordinary income
24 under the last sentence of subsection (a).”

1 (3) EFFECTIVE DATE.—The amendments made
2 by this subsection shall apply to sales of qualified se-
3 curities on or after the date of the enactment of this
4 Act.

5 (b) MODIFICATION TO 25-PERCENT SHAREHOLDER
6 RULE.—

7 (1) IN GENERAL.—Section 409(n)(1)(B) of
8 such Code is amended to read as follows:

9 “(B) for the benefit of any other person
10 who owns (after the application of section
11 318(a)) more than 25 percent of—

12 “(i) the total combined voting power
13 of all classes of stock of the corporation
14 which issued such employer securities or of
15 any corporation which is a member of the
16 same controlled group of corporations
17 (within the meaning of subsection (l)(4))
18 as such corporation, or

19 “(ii) the total value of all classes of
20 stock of any such corporation.”

21 (2) EFFECTIVE DATE.—The amendment made
22 by paragraph (1) shall take effect on the date of the
23 enactment of this Act.

1 **SEC. 4. ESOP DIVIDENDS MAY BE REINVESTED WITHOUT**
2 **LOSS OF DIVIDEND DEDUCTION.**

3 (a) **IN GENERAL.**—Section 404(k)(2)(A) of the Inter-
4 nal Revenue Code of 1986 (defining applicable dividends)
5 is amended by striking “or” at the end of clause (ii), by
6 redesignating clause (iii) as clause (iv), and by inserting
7 after clause (ii) the following new clause:

8 “(iii) is, at the election of such par-
9 ticipants or their beneficiaries—

10 “(I) payable as provided in clause
11 (i) or (ii), or

12 “(II) paid to the plan and rein-
13 vested in qualifying employer securi-
14 ties, or”.

15 (b) **EFFECTIVE DATE.**—The amendments made by
16 this section shall apply to taxable years beginning after
17 December 31, 1997.

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