

109TH CONGRESS
2D SESSION

S. 3857

To amend the Internal Revenue Code of 1986 to provide incentives to small businesses.

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 6, 2006

Mr. SMITH (for himself and Mrs. LINCOLN) 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 to provide incentives to small businesses.

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 “Bringing Opportunities
5 to Our Small Business Taxpayers Act” or “BOOST Act”.

1 **TITLE I—TAX FAIRNESS FOR**
2 **SMALL BUSINESSES**

3 **SEC. 101. PERMANENT EXTENSION OF EXPENSING FOR**
4 **SMALL BUSINESSES.**

5 (a) DOLLAR LIMITATION.—Paragraph (1) of section
6 179(b) of the Internal Revenue Code of 1986, as amended
7 by the Tax Increase Prevention and Reconciliation Act of
8 2005, is amended by striking “\$25,000 (\$100,000 in the
9 case of taxable years beginning after 2002 and before
10 2010)” and inserting “\$100,000”.

11 (b) REDUCTION IN LIMITATION.—Paragraph (2) of
12 section 179(b) of such Code, as amended by the Tax In-
13 crease Prevention and Reconciliation Act of 2005, is
14 amended by striking “\$200,000 (\$400,000 in the case of
15 taxable years beginning after 2002 and before 2010)” and
16 inserting “\$400,000”.

17 (c) INFLATION ADJUSTMENTS.—Subparagraph (A)
18 of section 179(b)(5) of such Code, as amended by the Tax
19 Increase Prevention and Reconciliation Act of 2005, is
20 amended by striking “and before 2010”.

21 (d) ELECTION.—Paragraph (2) of section 179(e) of
22 such Code, as amended by the Tax Increase Prevention
23 and Reconciliation Act of 2005, is amended by striking
24 “and before 2010”.

1 (e) COMPUTER SOFTWARE.—Clause (ii) of section
2 179(d)(1)(A), as amended by the Tax Increase Prevention
3 and Reconciliation Act of 2005, is amended by striking
4 “and before 2010”.

5 **SEC. 102. MODIFICATION OF CONSTRUCTION CONTRACTS**
6 **EXCEPTION TO PERCENTAGE OF COMPLE-**
7 **TION METHOD OF ACCOUNTING.**

8 (a) IN GENERAL.—Clause (ii) section 460(e)(1)(B)
9 of the Internal Revenue Code of 1986 is amended by strik-
10 ing “\$10,000,000” and inserting “\$25,000,000”.

11 (b) EFFECTIVE DATE.—The amendments made by
12 this section shall apply to contracts entered into after the
13 date of the enactment of this Act.

14 **SEC. 103. MODIFICATION OF LOOK-BACK METHOD FOR**
15 **CERTAIN CONSTRUCTION CONTRACTS.**

16 (a) IN GENERAL.—Subparagraph (B) of section
17 460(b)(3) of the Internal Revenue Code of 1986 is amend-
18 ed to read as follows:

19 “(B) LOOK-BACK METHOD NOT TO APPLY
20 TO CERTAIN CONTRACTS.—Paragraph (1)(B)
21 shall not apply to—

22 “(i) any construction contract which
23 is—

24 “(I) entered into by a taxpayer
25 whose average annual gross receipts

1 for the 3 taxable years preceding the
2 taxable year in which such contract is
3 completed do not exceed \$25,000,000,
4 and

5 “(II) completed within 3 years of
6 the contract commencement date, or

7 “(ii) any other contract—

8 “(I) the gross price of which (as
9 of the completion of the contract)
10 does not exceed the lesser of
11 \$1,000,000 or 1 percent of the aver-
12 age annual gross receipts of the tax-
13 payer for the 3 taxable years pre-
14 ceding the taxable year in which the
15 contract was completed, and

16 “(II) which is completed within 2
17 years of the contract commencement
18 date.

19 For purposes of this subparagraph, rules simi-
20 lar to the rules of subsections (e)(2) and (f)(3)
21 shall apply.”.

22 (b) EFFECTIVE DATE.—The amendments made by
23 this section shall apply to contracts completed in taxable
24 years ending after the date of the enactment of this Act.

1 **SEC. 104. USE OF CASH METHOD OF ACCOUNTING FOR CER-**
2 **TAIN SMALL BUSINESSES.**

3 (a) IN GENERAL.—Section 446 of the Internal Rev-
4 enue Code of 1986 is amended by adding at the end the
5 following new subsection:

6 “(g) USE OF CASH METHOD OF ACCOUNTING BY
7 CERTAIN TAXPAYERS.—

8 “(1) IN GENERAL.—Notwithstanding section
9 471 and subject to such regulations as the Secretary
10 may provide, a qualifying small business taxpayer
11 may use the cash receipts and disbursements method
12 of accounting.

13 “(2) QUALIFYING SMALL BUSINESS TAX-
14 PAYER.—For purposes of this subsection, the term
15 ‘qualifying small business taxpayer’ means a tax-
16 payer which—

17 “(A) meets the gross receipts test under
18 section 448(c) (determined by substituting
19 ‘\$10,000,000’ for ‘\$5,000,000’ each place it ap-
20 pears therein),

21 “(B) is not prohibited from using the cash
22 receipts and disbursement method of accounting
23 under section 448, and

24 “(C) meets the requirements described in
25 section 4.01 of Revenue Procedure 2002–28.”.

1 (b) EFFECTIVE DATE.—The amendments made by
 2 this section shall apply to taxable years beginning after
 3 the date of the enactment of this Act.

4 **TITLE II—S CORPORATION**
 5 **PARITY**

6 **SEC. 201. REDUCED RECOGNITION PERIOD FOR BUILT-IN**
 7 **GAINS.**

8 (a) IN GENERAL.—Paragraph (7) of section 1374(d)
 9 of the Internal Revenue Code of 1986 (relating to defini-
 10 tions and special rules) is amended to read as follows:

11 “(7) RECOGNITION PERIOD.—The term ‘rec-
 12 ognition period’ means the 7-year period beginning
 13 with the 1st day of the 1st taxable year for which
 14 the corporation was an S corporation. For purposes
 15 of applying this section to any amount includible in
 16 income by reason of distributions to shareholders
 17 pursuant to section 593(e), the preceding sentence
 18 shall be applied without regard to the duration of
 19 the recognition period in effect on the date of such
 20 distribution.”.

21 (b) EFFECTIVE DATE.—

22 (1) GENERAL RULE.—The amendment made by
 23 this section shall apply to any recognition period in
 24 effect on or after the date of the enactment of this
 25 Act.

1 rived from royalties, rents, dividends, interest,
2 and annuities.

3 “(B) EXCEPTION FOR INTEREST ON
4 NOTES FROM SALES OF INVENTORY.—The term
5 ‘passive investment income’ shall not include in-
6 terest on any obligation acquired in the ordi-
7 nary course of the corporation’s trade or busi-
8 ness from its sale of property described in sec-
9 tion 1221(a)(1).

10 “(C) TREATMENT OF CERTAIN LENDING
11 OR FINANCE COMPANIES.—If the S corporation
12 meets the requirements of section 542(c)(6) for
13 the taxable year, the term ‘passive investment
14 income’ shall not include gross receipts for the
15 taxable year which are derived directly from the
16 active and regular conduct of a lending or fi-
17 nance business (as defined in section
18 542(d)(1)).

19 “(D) TREATMENT OF CERTAIN DIVI-
20 DENDS.—If an S corporation holds stock in a
21 C corporation meeting the requirements of sec-
22 tion 1504(a)(2), the term ‘passive investment
23 income’ shall not include dividends from such C
24 corporation to the extent such dividends are at-
25 tributable to the earnings and profits of such C

1 corporation derived from the active conduct of
2 a trade or business.

3 “(E) EXCEPTION FOR BANKS, ETC.—In
4 the case of a bank (as defined in section 581),
5 a bank holding company (within the meaning of
6 section 2(a) of the Bank Holding Company Act
7 of 1956 (12 U.S.C. 1841(a))), or a financial
8 holding company (within the meaning of section
9 2(p) of such Act (12 U.S.C. 1841(p))), the
10 term ‘passive investment income’ shall not in-
11 clude—

12 “(i) interest income earned by such
13 bank or company, or

14 “(ii) dividends on assets required to
15 be held by such bank or company, includ-
16 ing stock in the Federal Reserve Bank, the
17 Federal Home Loan Bank, or the Federal
18 Agricultural Mortgage Bank or participa-
19 tion certificates issued by a Federal Inter-
20 mediate Credit Bank.

21 “(F) COORDINATION WITH SECTION
22 1374.—The amount of passive investment in-
23 come shall be determined by not taking into ac-
24 count any recognized built-in gain or loss of the
25 S corporation for any taxable year in the rec-

1 ognition period. Terms used in the preceding
2 sentence shall have the same respective mean-
3 ings as when used in section 1374.”.

4 (c) OTHER CONFORMING AMENDMENTS.—

5 (1) Subparagraph (J) of section 26(b)(2) of the
6 Internal Revenue Code of 1986 is amended by strik-
7 ing “25 percent” and inserting “60 percent”.

8 (2) Clause (i) of section 1042(c)(4)(A) of such
9 Code is amended by striking “section
10 1362(d)(3)(C)” and inserting “section 1375(b)(3)”.

11 (3) Subparagraph (B) of section 1362(f)(1) of
12 such Code is amended by striking “or (3)”.

13 (4) Clause (i) of section 1375(b)(1)(A) of such
14 Code is amended by striking “25 percent” and in-
15 serting “60 percent”.

16 (5) The heading for section 1375 of such Code
17 is amended by striking “**25 PERCENT**” and insert-
18 ing “**60 PERCENT**”.

19 (6) The item relating to section 1375 in the
20 table of sections for part III of subchapter S of
21 chapter 1 of such Code is amended by striking “25
22 percent” and inserting “60 percent”.

23 (d) EFFECTIVE DATE.—The amendments made by
24 this section shall apply to taxable years beginning after
25 the date of the enactment of this Act.

1 **SEC. 203. NONRESIDENT ALIENS ALLOWED TO BE SHARE-**
2 **HOLDERS.**

3 (a) NONRESIDENT ALIENS ALLOWED TO BE SHARE-
4 HOLDERS.—

5 (1) IN GENERAL.—Paragraph (1) of section
6 1361(b) of the Internal Revenue Code of 1986 (de-
7 fining small business corporation) is amended—

8 (A) by adding “and” at the end of sub-
9 paragraph (B),

10 (B) by striking subparagraph (C), and

11 (C) by redesignating subparagraph (D) as
12 subparagraph (C).

13 (2) CONFORMING AMENDMENTS.—

14 (A) Paragraph (4) and (5)(A) of section
15 1361(c) of such Code (relating to special rules
16 for applying subsection (b)) are each amended
17 by striking “subsection (b)(1)(D)” and insert-
18 ing “subsection (b)(1)(C)”.

19 (B) Clause (i) of section 280G(b)(5)(A) of
20 such Code (relating to general rule for exemp-
21 tion for small business corporations, etc.) is
22 amended by striking “but without regard to
23 paragraph (1)(C) thereof”.

24 (b) NONRESIDENT ALIEN SHAREHOLDER TREATED
25 AS ENGAGED IN TRADE OR BUSINESS WITHIN UNITED
26 STATES.—

1 (1) IN GENERAL.—Section 875 of the Internal
2 Revenue Code of 1986 is amended—

3 (A) by striking “and” at the end of para-
4 graph (1),

5 (B) by striking the period at the end of
6 paragraph (2) and inserting “, and”, and

7 (C) by adding at the end the following new
8 paragraph:

9 “(3) a nonresident alien individual shall be con-
10 sidered as being engaged in a trade or business
11 within the United States if the S corporation of
12 which such individual is a shareholder is so en-
13 gaged.”.

14 (2) PRO RATA SHARE OF S CORPORATION IN-
15 COME.—The last sentence of section 1441(b) of such
16 Code (relating to income items) is amended to read
17 as follows: “In the case of a nonresident alien indi-
18 vidual who is a member of a domestic partnership or
19 a shareholder of an S corporation, the items of in-
20 come referred to in subsection (a) shall be treated
21 as referring to items specified in this subsection in-
22 cluded in his distributive share of the income of such
23 partnership or in his pro rata share of the income
24 of such S corporation.”.

1 (3) APPLICATION OF WITHHOLDING TAX ON
2 NONRESIDENT ALIEN SHAREHOLDERS.—Section
3 1446 of such Code (relating to withholding tax on
4 foreign partners' share of effectively connected in-
5 come) is amended by redesignating subsection (f) as
6 subsection (g) and by inserting after subsection (e)
7 the following new subsection:

8 “(f) S CORPORATION TREATED AS PARTNERSHIP,
9 ETC.—For purposes of this section—

10 “(1) an S corporation shall be treated as a
11 partnership,

12 “(2) the shareholders of such corporation shall
13 be treated as partners of such partnership,

14 “(3) any reference to section 704 shall be treat-
15 ed as a reference to section 1366, and

16 “(4) no withholding tax under subsection (a)
17 shall be required in the case of any income realized
18 by such corporation and allocable to a shareholder
19 which is an electing small business trust (as defined
20 in section 1361(e)).”.

21 (4) CONFORMING AMENDMENTS.—

22 (A) The heading of section 875 of such
23 Code is amended to read as follows:

1 **“SEC. 875. PARTNERSHIPS; BENEFICIARIES OF ESTATES**
 2 **AND TRUSTS; S CORPORATIONS.”.**

3 (B) The heading of section 1446 of such
 4 Code is amended to read as follows:

5 **“SEC. 1446. WITHHOLDING TAX ON FOREIGN PARTNERS’**
 6 **AND S CORPORATION SHAREHOLDERS’**
 7 **SHARE OF EFFECTIVELY CONNECTED IN-**
 8 **COME.”.**

9 (5) CLERICAL AMENDMENTS.—

10 (A) The item relating to section 875 in the
 11 table of sections for subpart A of part II of
 12 subchapter N of chapter 1 of such Code is
 13 amended to read as follows:

“Sec. 875. Partnerships; beneficiaries of estates and trusts; S corporations.”.

14 (B) The item relating to section 1446 in
 15 the table of sections for subchapter A of chap-
 16 ter 3 of such Code is amended to read as fol-
 17 lows:

“Sec. 1446. Withholding tax on foreign partners’ and S corporation share-
 holders’ share of effectively connected income.”.

18 (C) PERMANENT ESTABLISHMENT OF
 19 PARTNERS AND S CORPORATION SHARE-
 20 HOLDERS.—Section 894 of such Code (relating
 21 to income affected by treaty) is amended by re-
 22 designating subsection (c) as subsection (d) and

1 by inserting after subsection (b) the following
2 new subsection:

3 “(c) PERMANENT ESTABLISHMENT OF PARTNERS
4 AND S CORPORATION SHAREHOLDERS.—If a partnership
5 or S corporation has a permanent establishment in the
6 United States (within the meaning of a treaty to which
7 the United States is a party) at any time during a taxable
8 year of such entity, a nonresident alien individual or for-
9 eign corporation which is a partner in such partnership,
10 or a nonresident alien individual who is a shareholder in
11 such S corporation, shall be treated as having a permanent
12 establishment in the United States for purposes of such
13 treaty.”.

14 (c) APPLICATION OF OTHER WITHHOLDING TAX
15 RULES ON NONRESIDENT ALIEN SHAREHOLDERS.—

16 (1) SECTION 1441.—Section 1441 of the Inter-
17 nal Revenue Code of 1986 (relating to withholding
18 of tax on nonresident aliens) is amended by redesign-
19 ating subsection (g) as subsection (h) and by in-
20 sserting after subsection (f) the following new sub-
21 section:

22 “(g) S CORPORATION TREATED AS PARTNERSHIP,
23 ETC.—For purposes of this section—

24 “(1) an S corporation shall be treated as a
25 partnership,

1 “(2) the shareholders of such corporation shall
2 be treated as partners of such partnership, and

3 “(3) no deduction or withholding under sub-
4 section (a) shall be required in the case of any item
5 of income realized by such corporation and allocable
6 to a shareholder which is an electing small business
7 trust (as defined in section 1361(e)).”.

8 (2) SECTION 1445.—Section 1445(e) of such
9 Code (relating to special rules relating to distribu-
10 tions, etc., by corporations, partnerships, trusts, or
11 estates) is amended by redesignating paragraph (6)
12 as paragraph (7) and by inserting after paragraph
13 (5) the following new paragraph:

14 “(6) S CORPORATION TREATED AS PARTNER-
15 SHIP, ETC.—For purposes of this section—

16 “(A) an S corporation shall be treated as
17 a partnership, and

18 “(B) the shareholders of such corporation
19 shall be treated as partners of such partnership,
20 and

21 “(C) no deduction or withholding under
22 subsection (a) shall be required in the case of
23 any gain realized by such corporation and allo-
24 cable to a shareholder which is an electing small
25 business trust (as defined in section 1361(e)).”.

1 (d) ADDITIONAL CONFORMING AMENDMENTS.—

2 (1) Section 1361(c)(2)(A)(i) of the Internal
3 Revenue Code of 1986 is amended by striking “who
4 is a citizen or resident of the United States”.

5 (2) Section 1361(d)(3)(B) of such Code is
6 amended by striking “who is a citizen or resident of
7 the United States”.

8 (3) Section 1361(e)(2) of such Code is amended
9 by inserting “(including a nonresident alien)” after
10 “person” the first place it appears.

11 (e) EFFECTIVE DATE.—The amendments made by
12 this section shall apply to taxable years beginning after
13 the date of the enactment of this Act.

14 **SEC. 204. EXPANSION OF S CORPORATION ELIGIBLE**
15 **SHAREHOLDERS TO INCLUDE IRAS.**

16 (a) IN GENERAL.—Clause (vi) of section
17 1361(c)(2)(A) of the Internal Revenue Code of 1986 (re-
18 lating to certain trusts permitted as shareholders) is
19 amended to read as follows:

20 “(vi) A trust which constitutes an in-
21 dividual retirement account under section
22 408(a), including one designated as a Roth
23 IRA under section 408A.”.

24 (b) SALE OF STOCK IN IRA RELATING TO S COR-
25 PORATION ELECTION EXEMPT FROM PROHIBITED

1 TRANSACTION RULES.—Paragraph (16) of section
2 4975(d) of the Internal Revenue Code of 1986 (relating
3 to exemptions) is amended to read as follows:

4 “(16) a sale of stock held by a trust which con-
5 stitutes an individual retirement account under sec-
6 tion 408(a) to the individual for whose benefit such
7 account is established if—

8 “(A) such sale is pursuant to an election
9 under section 1362(a) by the issuer of such
10 stock,

11 “(B) such sale is for fair market value at
12 the time of sale (as established by an inde-
13 pendent appraiser) and the terms of the sale
14 are otherwise at least as favorable to such trust
15 as the terms that would apply on a sale to an
16 unrelated party,

17 “(C) such trust does not pay any commis-
18 sions, costs, or other expenses in connection
19 with the sale, and

20 “(D) the stock is sold in a single trans-
21 action for cash not later than 120 days after
22 the S corporation election is made.”.

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

1 **TITLE III—PENSION PLAN**
2 **INCENTIVES AND PARITY**

3 **SEC. 301. CREDIT FOR QUALIFIED PENSION PLAN CON-**
4 **TRIBUTIONS OF SMALL EMPLOYERS.**

5 (a) **IN GENERAL.**—Subpart D of part IV of sub-
6 chapter A of chapter 1 of the Internal Revenue Code of
7 1986 (relating to business related credits) is amended by
8 adding at the end the following new section:

9 **“SEC. 45N. SMALL EMPLOYER PENSION PLAN CONTRIBU-**
10 **TIONS.**

11 “(a) **GENERAL RULE.**—For purposes of section 38,
12 in the case of an eligible employer, the small employer pen-
13 sion plan contribution credit determined under this section
14 for any taxable year is an amount equal to 50 percent
15 of the amount which would (but for subsection (f)(1)) be
16 allowed as a deduction under section 404 for such taxable
17 year for qualified employer contributions made to any
18 qualified retirement plan on behalf of any employee who
19 is not a highly compensated employee.

20 “(b) **CREDIT LIMITED TO 3 YEARS.**—The credit al-
21 lowable by this section shall be allowed only with respect
22 to the period of 3 taxable years beginning with the first
23 taxable year for which a credit is allowable with respect
24 to a plan under this section.

1 “(c) QUALIFIED EMPLOYER CONTRIBUTION.—For
2 purposes of this section—

3 “(1) DEFINED CONTRIBUTION PLANS.—In the
4 case of a defined contribution plan, the term ‘quali-
5 fied employer contribution’ means the amount of
6 nonelective and matching contributions to the plan
7 made by the employer on behalf of any employee
8 who is not a highly compensated employee to the ex-
9 tent such amount does not exceed 3 percent of such
10 employee’s compensation from the employer for the
11 year.

12 “(2) DEFINED BENEFIT PLANS.—In the case of
13 a defined benefit plan, the term ‘qualified employer
14 contribution’ means the amount of employer con-
15 tributions to the plan made on behalf of any em-
16 ployee who is not a highly compensated employee to
17 the extent that the accrued benefit of such employee
18 derived from employer contributions for the year
19 does not exceed the equivalent (as determined under
20 regulations prescribed by the Secretary and without
21 regard to contributions and benefits under the Social
22 Security Act) of 3 percent of such employee’s com-
23 pensation from the employer for the year.

24 “(d) QUALIFIED RETIREMENT PLAN.—

1 “(1) IN GENERAL.—The term ‘qualified retire-
2 ment plan’ means any plan described in section
3 401(a) which includes a trust exempt from tax
4 under section 501(a) if the plan meets—

5 “(A) the contribution requirements of
6 paragraph (2),

7 “(B) the vesting requirements of para-
8 graph (3), and

9 “(C) the distribution requirements of para-
10 graph (4).

11 “(2) CONTRIBUTION REQUIREMENTS.—

12 “(A) IN GENERAL.—The requirements of
13 this paragraph are met if, under the plan—

14 “(i) the employer is required to make
15 nonelective contributions of at least 1 per-
16 cent of compensation (or the equivalent
17 thereof in the case of a defined benefit
18 plan) for each employee who is not a high-
19 ly compensated employee who is eligible to
20 participate in the plan, and

21 “(ii) allocations of nonelective em-
22 ployer contributions, in the case of a de-
23 fined contribution plan, are either in equal
24 dollar amounts for all employees covered
25 by the plan or bear a uniform relationship

1 to the total compensation, or the basic or
2 regular rate of compensation, of the em-
3 ployees covered by the plan (and an equiv-
4 alent requirement is met with respect to a
5 defined benefit plan).

6 “(B) COMPENSATION LIMITATION.—The
7 compensation taken into account under sub-
8 paragraph (A) for any year shall not exceed the
9 limitation in effect for such year under section
10 401(a)(17).

11 “(3) VESTING REQUIREMENTS.—The require-
12 ments of this paragraph are met if the plan satisfies
13 the requirements of either of the following subpara-
14 graphs:

15 “(A) 3-YEAR VESTING.—A plan satisfies
16 the requirements of this subparagraph if an em-
17 ployee who has completed at least 3 years of
18 service has a nonforfeitable right to 100 percent
19 of the employee’s accrued benefit derived from
20 employer contributions.

21 “(B) 5-YEAR GRADED VESTING.—A plan
22 satisfies the requirements of this subparagraph
23 if an employee has a nonforfeitable right to a
24 percentage of the employee’s accrued benefit de-

1 rived from employer contributions determined
 2 under the following table:

“Years of service:	The nonforfeitable percentage is:
1	20
2	40
3	60
4	80
5	100.

3 “(4) DISTRIBUTION REQUIREMENTS.—In the
 4 case of a profit-sharing or stock bonus plan, the re-
 5 quirements of this paragraph are met if, under the
 6 plan, qualified employer contributions are distribut-
 7 able only as provided in section 401(k)(2)(B).

8 “(e) OTHER DEFINITIONS.—For purposes of this
 9 section—

10 “(1) ELIGIBLE EMPLOYER.—

11 “(A) IN GENERAL.—The term ‘eligible em-
 12 ployer’ means, with respect to any year, an em-
 13 ployer which has no more than 25 employees
 14 who received at least \$5,000 of compensation
 15 from the employer for the preceding year.

16 “(B) REQUIREMENT FOR NEW QUALIFIED
 17 EMPLOYER PLANS.—Such term shall not in-
 18 clude an employer if, during the 3-taxable year
 19 period immediately preceding the 1st taxable
 20 year for which the credit under this section is
 21 otherwise allowable for a qualified employer
 22 plan of the employer, the employer or any mem-

1 ber of any controlled group including the em-
2 ployer (or any predecessor of either) established
3 or maintained a qualified employer plan with
4 respect to which contributions were made, or
5 benefits were accrued, for substantially the
6 same employees as are in the qualified employer
7 plan.

8 “(2) HIGHLY COMPENSATED EMPLOYEE.—The
9 term ‘highly compensated employee’ has the mean-
10 ing given such term by section 414(q) (determined
11 without regard to section 414(q)(1)(B)(ii)).

12 “(f) SPECIAL RULES.—

13 “(1) DISALLOWANCE OF DEDUCTION.—No de-
14 duction shall be allowed for that portion of the quali-
15 fied employer contributions paid or incurred for the
16 taxable year which is equal to the credit determined
17 under subsection (a).

18 “(2) ELECTION NOT TO CLAIM CREDIT.—This
19 section shall not apply to a taxpayer for any taxable
20 year if such taxpayer elects to have this section not
21 apply for such taxable year.

22 “(3) AGGREGATION RULES.—All persons treat-
23 ed as a single employer under subsection (a) or (b)
24 of section 52, or subsection (n) or (o) of section 414,

1 shall be treated as one person. All eligible employer
2 plans shall be treated as 1 eligible employer plan.

3 “(g) RECAPTURE OF CREDIT ON FORFEITED CON-
4 TRIBUTIONS.—

5 “(1) IN GENERAL.—Except as provided in para-
6 graph (2), if any accrued benefit which is forfeitable
7 by reason of subsection (d)(3) is forfeited, the em-
8 ployer’s tax imposed by this chapter for the taxable
9 year in which the forfeiture occurs shall be increased
10 by 35 percent of the employer contributions from
11 which such benefit is derived to the extent such con-
12 tributions were taken into account in determining
13 the credit under this section.

14 “(2) REALLOCATED CONTRIBUTIONS.—Para-
15 graph (1) shall not apply to any contribution which
16 is reallocated by the employer under the plan to em-
17 ployees who are not highly compensated employees.”.

18 (b) CREDIT ALLOWED AS PART OF GENERAL BUSI-
19 NESS CREDIT.—Section 38(b) of the Internal Revenue
20 Code of 1986 (defining current year business credit) is
21 amended by striking “plus” at the end of paragraph (29),
22 by striking the period at the end of paragraph (30) and
23 inserting “, plus”, and by adding at the end the following
24 new paragraph:

1 “(31) in the case of an eligible employer (as de-
 2 fined in section 45E(e)), the small employer pension
 3 plan contribution credit determined under section
 4 45M(a).”

5 (c) CONFORMING AMENDMENTS.—

6 (1) Subsection (c) of section 196 of the Internal
 7 Revenue Code of 1986 is amended by striking “and”
 8 at the end of paragraph (12), by striking the period
 9 at the end of paragraph (13) and inserting “, and”,
 10 and by adding at the end the following new para-
 11 graph:

12 “(14) the small employer pension plan contribu-
 13 tion credit determined under section 45E(a).”

14 (2) The table of sections for subpart D of part
 15 IV of subchapter A of chapter 1 of such Code is
 16 amended by adding at the end the following new
 17 item:

“Sec. 45M. Small employer pension plan contributions.”.

18 (d) EFFECTIVE DATE.—The amendments made by
 19 this section shall apply to contributions paid or incurred
 20 in taxable years beginning after December 31, 2006.

21 **SEC. 302. DEDUCTION FOR PENSION CONTRIBUTIONS AL-**
 22 **LOWED IN COMPUTING NET EARNINGS FROM**
 23 **SELF-EMPLOYMENT.**

24 (a) IN GENERAL.—Section 1402(a) of the Internal
 25 Revenue Code of 1986 (defining net earnings from self-

1 employment) is amended by striking “and” at the end of
2 paragraph (15), by striking the period at the end of para-
3 graph (16) and inserting “, and”, and by inserting after
4 paragraph (16) the following new paragraph:

5 “(17) any deduction allowed under section 404
6 by reason of section 404(a)(8)(C) shall be allowed,
7 except that the amount of such deduction shall be
8 determined without regard to this paragraph.”.

9 (b) EFFECTIVE DATE.—The amendments made by
10 this section shall apply to taxable years beginning after
11 December 31, 2006.

12 **TITLE IV—HEALTH INSURANCE** 13 **COSTS PARITY**

14 **SEC. 401. DEDUCTION FOR HEALTH INSURANCE COSTS AL-** 15 **LOWED IN COMPUTING NET EARNINGS FROM** 16 **SELF-EMPLOYMENT.**

17 (a) IN GENERAL.—Section 1402(a) of the Internal
18 Revenue Code of 1986 (defining net earnings from self-
19 employment), as amended by section 302, is amended by
20 striking “and” at the end of paragraph (16), by striking
21 the period at the end of paragraph (17) and inserting “,
22 and”, and by inserting after paragraph (17) the following
23 new paragraph:

24 “(18) any deduction allowed under section
25 162(l) shall be allowed.”.

1 (b) CONFORMING AMENDMENT.—Section 162(l) of
2 the Internal Revenue Code of 1986 (relating to special
3 rule for health insurance costs of self-employed individ-
4 uals) is amended by striking paragraph (4) and by redes-
5 ignating paragraph (5) as paragraph (4).

6 (c) EFFECTIVE DATE.—The amendments made by
7 this section shall apply to taxable years beginning after
8 December 31, 2006.

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