

103^D CONGRESS
2^D SESSION

H. R. 4269

To amend the Internal Revenue Code of 1986 to reduce the tax on capital gains of individuals, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

APRIL 20, 1994

Mr. SMITH of Texas introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to reduce the tax on capital gains of individuals, and for other purposes.

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 “Economic Investment
5 and Savings Incentive Act”.

6 **SEC. 2. REDUCTION IN CAPITAL GAINS TAX FOR INDIVID-**
7 **UALS.**

8 (a) GENERAL RULE.—Part I of subchapter P of
9 chapter 1 of the Internal Revenue Code of 1986 (relating

1 to treatment of capital gains) is amended by adding at
2 the end thereof the following new section:

3 **“SEC. 1203. DEDUCTION FOR CAPITAL GAINS.**

4 “(a) ALLOWANCE OF DEDUCTION.—If, for any tax-
5 able year, a taxpayer other than a corporation has a net
6 capital gain, there shall be allowed as a deduction from
7 gross income for such taxable year an amount equal to
8 the sum of—

9 “(1) 60 percent of the 3-year capital gain,

10 “(2) 40 percent of the 2-year capital gain, and

11 “(3) 20 percent of the 1-year capital gain.

12 “(b) TRANSITIONAL RULES.—

13 “(1) YEARS BEGINNING IN 1994.—In the case of
14 a taxable year beginning in 1994, the deduction
15 under subsection (a) shall be 60 percent of the net
16 capital gain.

17 “(2) YEARS BEGINNING IN 1995.—In the case of
18 a taxable year beginning in 1995, the deduction
19 under subsection (a) shall be the sum of—

20 “(A) 60 percent of the 3-year capital gain
21 and the 2-year capital gain, and

22 “(B) 40 percent of the 1-year capital gain.

23 “(c) DEFINITIONS.—For purposes of this section:

24 “(1) 3-YEAR CAPITAL GAIN.—The term ‘3-year
25 capital gain’ means the lesser of—

1 “(A) the net capital gain for the taxable
2 year, or

3 “(B) the long-term capital gain determined
4 by only taking into account gain from the sale
5 or exchange of assets held for more than 3
6 years.

7 “(2) 2-YEAR CAPITAL GAIN.—The term ‘2-year
8 capital gain’ means the lesser of—

9 “(A) the net capital gain for the taxable
10 year reduced by the 3-year capital gain, or

11 “(B) the long-term capital gain determined
12 by only taking into account gain from the sale
13 or exchange of assets held for more than 2
14 years but not more than 3 years.

15 “(3) 1-YEAR CAPITAL GAIN.—The term ‘1-year
16 capital gain’ means the net capital gains for the tax-
17 able year reduced by the 3-year capital gain and the
18 2-year capital gain.

19 “(4) RECAPTURE OF NET ORDINARY LOSS
20 UNDER SECTION 1231.—For purposes of this sub-
21 section, if any amount is treated as ordinary income
22 under section 1231(c) for any taxable year—

23 “(A) the amount so treated shall be allo-
24 cated proportionately among the section 1231

1 gains (as defined in section 1231(a)) for such
2 taxable year, and

3 “(B) the amount so allocated to any such
4 gain shall reduce the amount of such gain.

5 “(c) ESTATE AND TRUSTS.—In the case of an estate
6 or trust, the deduction under this section shall be com-
7 puted by excluding the portion (if any) of the gains for
8 the taxable year from sales or exchanges of capital assets
9 which, under sections 652 and 662 (relating to inclusions
10 of amounts in gross income of beneficiaries of trusts), is
11 includable by the income beneficiaries as gain derived from
12 the sale or exchange of capital assets.”

13 (b) TREATMENT OF COLLECTIBLES.—

14 (1) IN GENERAL.—Section 1222 of such Code
15 is amended by inserting after paragraph (11) the
16 following new paragraph:

17 “(12) SPECIAL RULE FOR COLLECTIBLES.—

18 “(A) IN GENERAL.—Any gain or loss from
19 the sale or exchange of a collectible shall be
20 treated as a short-term capital gain or loss (as
21 the case may be), without regard to the period
22 such asset was held. The preceding sentence
23 shall apply only to the extent the gain or loss
24 is taken into account in computing taxable in-
25 come.

1 “(B) TREATMENT OF CERTAIN SALES OF
2 INTEREST IN PARTNERSHIP, ETC.—For pur-
3 poses of subparagraph (A), any gain from the
4 sale or exchange of an interest in a partnership,
5 S corporation, or trust which is attributable to
6 unrealized appreciation in the value of collect-
7 ibles held by such entity shall be treated as gain
8 from the sale or exchange of a collectible. Rules
9 similar to the rules of section 751(f) shall apply
10 for purposes of the preceding sentence.

11 “(C) COLLECTIBLE.—For purposes of this
12 paragraph, the term ‘collectible’ means any cap-
13 ital asset which is a collectible (as defined in
14 section 408(m) without regard to paragraph (3)
15 thereof).”

16 (2) CHARITABLE DEDUCTION NOT AF-
17 FECTED.—

18 (A) Paragraph (1) of section 170(e) is
19 amended by adding at the end thereof the fol-
20 lowing new sentence: “For purposes of this
21 paragraph, section 1222 shall be applied with-
22 out regard to paragraph (12) thereof (relating
23 to special rule for collectibles).”

24 (B) Clause (iv) of section 170(b)(1)(C) is
25 amended by inserting before the period at the

1 end thereof the following: “and section 1222
2 shall be applied without regard to paragraph
3 (12) thereof (relating to special rule for collect-
4 ibles)”.

5 (c) MINIMUM TAX.—Section 56(b) of such Code is
6 amended by adding at the end thereof the following new
7 paragraph:

8 “(4) CAPITAL GAINS DEDUCTION ALLOWED.—
9 The deduction under section 1203 shall be allowed.”

10 (d) CONFORMING AMENDMENTS.—

11 (1) Subsection (h) of section 1 of such Code is
12 hereby repealed.

13 (2) Section 62(a) of such Code is amended by
14 inserting after paragraph (15) the following new
15 paragraph:

16 “(16) CAPITAL GAINS DEDUCTION.—The deduc-
17 tion allowed by section 1203.”

18 (3) Subparagraph (B) of section 163(d)(4) is
19 amended by striking clauses (i), (ii), and (iii) and in-
20 sserting the following:

21 “(i) gross income from property held
22 for investment (other than any gain taken
23 into account under clause (ii)), and

24 “(ii) any net gain attributable to the
25 disposition of property held for investment

1 reduced by any deduction allowable under
2 section 1203 attributable to gain from
3 such property.”

4 (4)(A) Section 170(e)(1)(B) of such Code is
5 amended by inserting “(or, in the case of a taxpayer
6 other than a corporation, the nondeductible percent-
7 age of the amount of gain)” after “the amount of
8 gain”.

9 (B) Section 170(e)(1) of such Code is amended
10 by adding at the end thereof the following new sen-
11 tence: “For purposes of subparagraph (B), the term
12 ‘nondeductible percentage’ means 100 percent minus
13 the applicable percentage with respect to such prop-
14 erty under section 1203(c).”

15 (5) Subparagraph (B) of section 172(d)(2) of
16 such Code is amended by inserting “, and the deduc-
17 tion provided by section 1203,” after “section
18 1202”.

19 (6)(A) Section 220 of such Code (relating to
20 cross reference) is amended to read as follows:

21 **“SEC. 220. CROSS REFERENCES.**

“(1) For deduction for net capital gain, see section 1203.

“(2) For deductions in respect of a decedent, see section 691.”

22 (B) The table of sections for part VII of sub-
23 chapter B of chapter 1 of such Code is amended by

1 striking “reference” in the item relating to section
2 220 and inserting “references”.

3 (7) Paragraph (4) of section 642(c) of such
4 Code is amended to read as follows:

5 “(4) ADJUSTMENTS.—To the extent that the
6 amount otherwise allowable as a deduction under
7 this subsection consists of gain from the sale or ex-
8 change of capital assets held for more than 1 year,
9 proper adjustment shall be made for any exclusion
10 allowable to the estate or trust under section 1202
11 and for any deduction allowable to the estate or
12 trust under section 1203. In the case of a trust, the
13 deduction allowed by this subsection shall be subject
14 to section 681 (relating to unrelated business in-
15 come).”

16 (8) Paragraph (3) of section 643(a) of such
17 Code is amended by inserting “, and the deduction
18 under section 1203,” after “section 1202”.

19 (9) Paragraph (6)(C) of section 643(a) of such
20 Code is amended—

21 (A) by inserting “(i)” before “there”, and

22 (B) by inserting “, and (ii) the deduction
23 under section 1203 (relating to deduction for
24 excess of capital gains over capital losses) shall

1 not be taken into account” before the period at
2 the end thereof.

3 (10) Paragraph (4) of section 691(c) of such
4 Code is amended—

5 (A) by striking “1(h),” , and

6 (B) by inserting “1203,” after “1202,”.

7 (11) The second sentence of paragraph (2) of
8 section 871(a) of such Code is amended by striking
9 “section 1202” and inserting “sections 1202 and
10 1203”.

11 (12)(A) Subparagraph (B) of section 904(b)(2)
12 of such Code is amended by striking out so much of
13 such subparagraph as precedes clause (i) and insert-
14 ing the following:

15 “(B) SPECIAL RULES WHERE CORPORATE
16 CAPITAL RATE GAIN DIFFERENTIAL.—In the
17 case of a corporation, for any taxable
18 year for which there is a capital gain rate dif-
19 ferential—”.

20 (B) Subparagraphs (D) and (E) of section
21 904(b)(3) of such Code are amended to read as fol-
22 lows:

23 “(D) CAPITAL GAIN RATE DIFFEREN-
24 TIAL.—There is a capital gain rate differential
25 for any taxable year if any rate of tax imposed

1 by section 11, 511, or 831(a) or (b) (whichever
2 applies) exceeds the alternative rate of tax
3 under section 1201(a) (determined without re-
4 gard to the last sentence of section 11(b)(1)).

5 “(E) RATE DIFFERENTIAL PORTION.—The
6 rate differential portion of foreign source net
7 capital gain, net capital, or the excess of net
8 capital gain from sources within the United
9 States over net capital gain, as the case may
10 be, is the same proportion of such amount as—

11 “(i) the excess of the highest rate of
12 tax specified in section 11(b)(1) over the
13 alternative rate of tax under section
14 1201(a), bears to

15 “(ii) the highest rate of tax specified
16 in section 11(b)(1).”

17 (13) Section 1402(i)(1) is amended to read as
18 follows:

19 “(1) IN GENERAL.—In determining the net
20 earnings from self-employment of any options dealer
21 or commodities dealer—

22 “(A) notwithstanding subsection (a)(3)(A),
23 there shall not be excluded any gain or loss (in
24 the normal course of the taxpayer’s activity of
25 dealing in or trading section 1256 contracts)

1 from section 1256 contracts or property related
2 to such contracts, and

3 “(B) the deduction provided by section
4 1203 shall not apply.”

5 (e) CLERICAL AMENDMENT.—The table of sections
6 for part I of subchapter P of chapter 1 is amended by
7 adding at the end thereof the following new item:

“Sec. 1203. Deduction for capital gains.”

8 (f) EFFECTIVE DATE.—The amendments made by
9 this section shall apply to taxable years beginning after
10 December 31, 1993.

11 **SEC. 3. INDEXING OF CERTAIN ASSETS ACQUIRED ON OR**
12 **AFTER JANUARY 1, 1997, FOR PURPOSES OF**
13 **DETERMINING GAIN.**

14 (a) IN GENERAL.—Part II of subchapter O of chap-
15 ter 1 of the Internal Revenue Code of 1986 (relating to
16 basis rules of general application) is amended by inserting
17 after section 1021 the following new section:

18 **“SEC. 1022. INDEXING OF CERTAIN ASSETS ACQUIRED ON**
19 **OR AFTER JANUARY 1, 1997, FOR PURPOSES**
20 **OF DETERMINING GAIN.**

21 “(a) GENERAL RULE.—

22 “(1) INDEXED BASIS SUBSTITUTED FOR AD-
23 JUSTED BASIS.—Solely for purposes of determining
24 gain on the sale or other disposition by a taxpayer
25 (other than a corporation) of an indexed asset which

1 has been held for more than 1 year, the indexed
2 basis of the asset shall be substituted for its ad-
3 justed basis.

4 “(2) SPECIAL RULE FOR RECAPTURE GAIN.—

5 “(A) IN GENERAL.—Paragraph (1) shall
6 not apply for purposes of determining the
7 amount of recapture gain on the sale or other
8 disposition of an indexed asset, but the amount
9 of any such recapture gain shall increase the
10 adjusted basis of the asset for purposes of ap-
11 plying paragraph (1) to determine the amount
12 of other gain on such sale or other disposition.

13 “(B) RECAPTURE GAIN.—For purposes of
14 subparagraph (A), the term ‘recapture gain’
15 means any gain treated as ordinary income
16 under section 1245, 1250, or 1254 and any
17 gain which would have been treated as ordinary
18 income under section 1250 if such section ap-
19 plied to all depreciation adjustments instead of
20 only additional depreciation.

21 “(b) INDEXED ASSET.—

22 “(1) IN GENERAL.—For purposes of this sec-
23 tion, the term ‘indexed asset’ means—

24 “(A) any stock in a corporation, and

1 “(B) any tangible property (or any interest
2 therein),
3 which is a capital asset or property used in the trade
4 or business (as defined in section 1231(b)) and the
5 holding period of which begins on or after January
6 1, 1997.

7 “(2) CERTAIN PROPERTY EXCLUDED.—For
8 purposes of this section, the term ‘indexed asset’
9 does not include—

10 “(A) CREDITOR’S INTEREST.—Any interest
11 in property which is in the nature of a credi-
12 tor’s interest.

13 “(B) COLLECTIBLES.—Any collectible (as
14 defined in section 408(m)(2) without regard to
15 section 408(m)(3)).

16 “(C) OPTIONS.—Any option or other right
17 to acquire an interest in property.

18 “(D) NET LEASE PROPERTY.—In the case
19 of a lessor, net lease property (within the mean-
20 ing of subsection (i)(3)).

21 “(E) STOCK IN FOREIGN CORPORA-
22 TIONS.—Stock in a foreign corporation.

23 “(F) STOCK IN S CORPORATIONS.—Stock
24 in an S corporation.

1 “(3) EXCEPTION FOR STOCK IN FOREIGN COR-
2 PORATION WHICH IS REGULARLY TRADED ON NA-
3 TIONAL OR REGIONAL EXCHANGE.—Paragraph
4 (2)(E) shall not apply to stock in a foreign corpora-
5 tion the stock of which is listed on the New York
6 Stock Exchange, the American Stock Exchange, or
7 any domestic regional exchange for which quotations
8 are published on a regular basis or is authorized for
9 trading on the national market system operated by
10 the National Association of Securities Dealers other
11 than—

12 “(A) a passive foreign corporation (as de-
13 fined in section 1296), and

14 “(B) stock in a foreign corporation held by
15 a United States person who meets the require-
16 ments of section 1248(a)(2).

17 “(c) INDEXED BASIS.—For purposes of this section:

18 “(1) INDEXED BASIS.—The indexed basis for
19 any asset is—

20 “(A) the adjusted basis of the asset, multi-
21 plied by

22 “(B) the applicable inflation ratio.

23 “(2) APPLICABLE INFLATION RATIO.—The ap-
24 plicable inflation ratio for any asset shall be deter-
25 mined by dividing—

1 “(A) the CPI for the calendar year preced-
2 ing the calendar year in which the disposition
3 takes place, by

4 “(B) the CPI for the calendar year preced-
5 ing the calendar year in which the taxpayer’s
6 holding period for such asset began.

7 The applicable inflation ratio shall not be taken into
8 account unless it is greater than 1. The applicable
9 inflation ratio for any asset shall be rounded to the
10 nearest one-thousandth.

11 “(3) CONVENTIONS.—For purposes of para-
12 graph (2), if any asset is disposed of during any cal-
13 endar year—

14 “(A) such disposition shall be treated as
15 occurring on the last day of such calendar year,
16 and

17 “(B) the taxpayer’s holding period for such
18 asset shall be treated as beginning in the same
19 calendar year as would be determined for an
20 asset actually disposed of on such last day with
21 a holding period of the same length as the ac-
22 tual holding period of the asset involved.

23 “(4) CPI.—For purposes of this subsection, the
24 CPI for any calendar year shall be determined under
25 section 1(f)(4).

1 “(d) SHORT SALES.—

2 “(1) IN GENERAL.—In the case of a short sale
3 of an indexed asset with a short sale period in excess
4 of 1 year, for purposes of this title, the amount real-
5 ized shall be an amount equal to the amount realized
6 (determined without regard to this paragraph) mul-
7 tiplied by the applicable inflation ratio. In applying
8 subsection (c)(2) for purposes of the preceding sen-
9 tence, the date on which the property is sold short
10 shall be treated as the date on which the holding pe-
11 riod for the asset begins and the closing date for the
12 sale shall be treated as the date of disposition.

13 “(2) SHORT SALE OF SUBSTANTIALLY IDEN-
14 TICAL PROPERTY.—If the taxpayer or the taxpayer’s
15 spouse sells short property substantially identical to
16 an asset held by the taxpayer, the asset held by the
17 taxpayer and the substantially identical property
18 shall not be treated as indexed assets for the short
19 sale period.

20 “(3) SHORT SALE PERIOD.—For purposes of
21 this subsection, the short sale period begins on the
22 day after property is sold and ends on the closing
23 date for the sale.

24 “(e) TREATMENT OF REGULATED INVESTMENT
25 COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

1 “(1) ADJUSTMENTS AT ENTITY LEVEL.—

2 “(A) IN GENERAL.—Except as otherwise
3 provided in this paragraph, the adjustment
4 under subsection (a) shall be allowed to any
5 qualified investment entity (including for pur-
6 poses of determining the earnings and profits of
7 such entity).

8 “(B) EXCEPTION FOR CORPORATE SHARE-
9 HOLDERS.—Under regulations—

10 “(i) in the case of a distribution by a
11 qualified investment entity (directly or in-
12 directly) to a corporation—

13 “(I) the determination of whether
14 such distribution is a dividend shall be
15 made without regard to this section,
16 and

17 “(II) the amount treated as gain
18 by reason of the receipt of any capital
19 gain dividend shall be increased by the
20 percentage by which the entity’s net
21 capital gain for the taxable year deter-
22 mined without regard to this section
23 exceeds the entity’s net capital gain
24 for such year determined with regard
25 to this section, and

1 “(ii) there shall be other appropriate
2 adjustments (including deemed distribu-
3 tions) so as to ensure that the benefits of
4 this section are not allowed (directly or in-
5 directly) to corporate shareholders of quali-
6 fied investment entities.

7 For purposes of the preceding sentence, any
8 amount includible in gross income under section
9 852(b)(3)(D) shall be treated as a capital gain
10 dividend and an S corporation shall not be
11 treated as a corporation.

12 “(C) EXCEPTION FOR QUALIFICATION
13 PURPOSES.—This section shall not apply for
14 purposes of sections 851(b) and 856(c).

15 “(D) EXCEPTION FOR CERTAIN TAXES IM-
16 POSED AT ENTITY LEVEL.—

17 “(i) TAX ON FAILURE TO DISTRIBUTE
18 ENTIRE GAIN.—If any amount is subject to
19 tax under section 852(b)(3)(A) for any
20 taxable year, the amount on which tax is
21 imposed under such section shall be in-
22 creased by the percentage determined
23 under subparagraph (B)(i)(II). A similar
24 rule shall apply in the case of any amount
25 subject to tax under paragraph (2) or (3)

1 of section 857(b) to the extent attributable
2 to the excess of the net capital gain over
3 the deduction for dividends paid deter-
4 mined with reference to capital gain divi-
5 dends only. The first sentence of this
6 clause shall not apply to so much of the
7 amount subject to tax under section
8 852(b)(3)(A) as is designated by the com-
9 pany under section 852(b)(3)(D).

10 “(ii) OTHER TAXES.—This section
11 shall not apply for purposes of determining
12 the amount of any tax imposed by para-
13 graph (4), (5), or (6) of section 857(b).

14 “(2) ADJUSTMENTS TO INTERESTS HELD IN
15 ENTITY.—

16 “(A) IN GENERAL.—Stock in a qualified
17 investment entity shall be an indexed asset for
18 any calendar month in the same ratio as the
19 fair market value of the assets held by such en-
20 tity at the close of such month which are in-
21 dexed assets (determined without regard to the
22 requirement that the holding period begin on or
23 after January 1, 1997) bears to the fair market
24 value of all assets of such entity at the close of
25 such month.

1 “(B) RATIO OF 90 PERCENT OR MORE.—If
2 the ratio for any calendar month determined
3 under subparagraph (A) would (but for this
4 subparagraph) be 90 percent or more, such
5 ratio for such month shall be 100 percent.

6 “(C) RATIO OF 10 PERCENT OR LESS.—If
7 the ratio for any calendar month determined
8 under subparagraph (A) would (but for this
9 subparagraph) be 10 percent or less, such ratio
10 for such month shall be zero.

11 “(D) VALUATION OF ASSETS IN CASE OF
12 REAL ESTATE INVESTMENT TRUSTS.—Nothing
13 in this paragraph shall require a real estate in-
14 vestment trust to value its assets more fre-
15 quently than once each 36 months (except
16 where such trust ceases to exist). The ratio
17 under subparagraph (A) for any calendar
18 month for which there is no valuation shall be
19 the trustee’s good faith judgment as to such
20 valuation.

21 “(3) QUALIFIED INVESTMENT ENTITY.—For
22 purposes of this subsection, the term ‘qualified in-
23 vestment entity’ means—

24 “(A) a regulated investment company
25 (within the meaning of section 851), and

1 “(B) a real estate investment trust (within
2 the meaning of section 856).

3 “(f) OTHER PASS-THRU ENTITIES.—

4 “(1) PARTNERSHIPS.—

5 “(A) IN GENERAL.—In the case of a part-
6 nership, the adjustment made under subsection
7 (a) at the partnership level shall be passed
8 through to the partners (but only for purposes
9 of determining the income of partners who are
10 not corporations).

11 “(B) SPECIAL RULE IN THE CASE OF SEC-
12 TION 754 ELECTIONS.—In the case of a transfer
13 of an interest in a partnership with respect to
14 which the election provided in section 754 is in
15 effect—

16 “(i) the adjustment under section
17 743(b)(1) shall, with respect to the trans-
18 feror partner, be treated as a sale of the
19 partnership assets for purposes of applying
20 this section, and

21 “(ii) with respect to the transferee
22 partner, the partnership’s holding period
23 for purposes of this section in such assets
24 shall be treated as beginning on the date
25 of such adjustment.

1 “(2) S CORPORATIONS.—In the case of an S
2 corporation, the adjustment made under subsection
3 (a) at the corporate level shall be passed through to
4 the shareholders. This section shall not apply for
5 purposes of determining the amount of any tax im-
6 posed by section 1374 or 1375.

7 “(3) COMMON TRUST FUNDS.—In the case of a
8 common trust fund, the adjustment made under sub-
9 section (a) at the trust level shall be passed through
10 to the participants (but only for purposes of deter-
11 mining the income of participants who are not cor-
12 porations).

13 “(g) DISPOSITIONS BETWEEN RELATED PERSONS.—
14 This section shall not apply to any sale or other disposition
15 of property between related persons (within the meaning
16 of section 465(b)(3)(C)) if such property, in the hands of
17 the transferee, is of a character subject to the allowance
18 for depreciation provided in section 167.

19 “(h) TRANSFERS TO INCREASE INDEXING ADJUST-
20 MENT.—If any person transfers cash, debt, or any other
21 property to another person and the principal purpose of
22 such transfer is to secure or increase an adjustment under
23 subsection (a), the Secretary may disallow part or all of
24 such adjustment or increase.

25 “(i) SPECIAL RULES.—For purposes of this section:

1 “(1) TREATMENT AS SEPARATE ASSET.—In the
2 case of any asset, the following shall be treated as
3 a separate asset:

4 “(A) A substantial improvement to prop-
5 erty.

6 “(B) In the case of stock of a corporation,
7 a substantial contribution to capital.

8 “(C) Any other portion of an asset to the
9 extent that separate treatment of such portion
10 is appropriate to carry out the purposes of this
11 section.

12 “(2) ASSETS WHICH ARE NOT INDEXED ASSETS
13 THROUGHOUT HOLDING PERIOD.—The applicable in-
14 flation ratio shall be appropriately reduced for peri-
15 ods during which the asset was not an indexed asset.

16 “(3) NET LEASE PROPERTY DEFINED.—The
17 term ‘net lease property’ means leased property
18 where—

19 “(A) the term of the lease (taking into ac-
20 count options to renew) was 50 percent or more
21 of the useful life of the property, and

22 “(B) for the period of the lease, the sum
23 of the deductions with respect to such property
24 which are allowable to the lessor solely by rea-
25 son of section 162 (other than rents and reim-

1 bursed amounts with respect to such property)
2 is 15 percent or less of the rental income pro-
3 duced by such property.

4 “(j) REGULATIONS.—The Secretary shall prescribe
5 such regulations as may be necessary or appropriate to
6 carry out the purposes of this section.”

7 (b) GAINS AND LOSSES FROM INDEXED ASSETS NOT
8 TAKEN INTO ACCOUNT UNDER LIMITATION ON INVEST-
9 MENT INTEREST.—Subparagraph (B) of section
10 163(d)(4) of such Code (defining investment income) is
11 amended by adding at the end thereof the following new
12 sentences:

13 “Gain from the sale or other disposition of an in-
14 dexed asset (as defined in section 1022) held for
15 more than 1 year shall not be taken into account for
16 purposes of the preceding sentence. The preceding
17 sentence shall not apply to gain from the sale or
18 other disposition of any such asset if the taxpayer
19 elects to waive the benefits of section 1022 in deter-
20 mining the amount of such gain.”

21 (c) CLERICAL AMENDMENT.—The table of sections
22 for part II of subchapter O of chapter 1 of such Code
23 is amended by inserting after the item relating to section
24 1021 the following new item:

“Sec. 1022. Indexing of certain assets acquired on or after Janu-
ary 1, 1997, for purposes of determining gain.”

1 (d) EFFECTIVE DATE.—

2 (1) IN GENERAL.—The amendments made by
3 this section shall apply to the disposition of any
4 property the holding period of which begins on or
5 after January 1, 1997.

6 (2) CERTAIN TRANSACTIONS BETWEEN RELAT-
7 ED PERSONS.—The amendments made by this sec-
8 tion shall not apply to the disposition of any prop-
9 erty acquired on or after January 1, 1997, from a
10 related person (as defined in section 465(b)(3)(C) of
11 the Internal Revenue Code of 1986) if—

12 (A) such property was so acquired for a
13 price less than the property's fair market value,
14 and

15 (B) the amendments made by this section
16 did not apply to such property in the hands of
17 such related person.

18 (e) ELECTION TO RECOGNIZE GAIN ON READILY
19 TRADEABLE SECURITIES HELD ON JANUARY 1, 1997.—

20 (1) IN GENERAL.—If a taxpayer other than a
21 corporation holds any readily tradable security on
22 January 1, 1997, the taxpayer may elect to treat
23 such security as having been sold on the last busi-
24 ness day before such date for an amount equal to its
25 closing market price on such last business day (and

1 as having been reacquired on such last business day
2 for an amount equal to such closing market price).

3 (2) TREATMENT OF GAIN OR LOSS.—

4 (A) Any gain resulting from an election
5 under paragraph (1) shall be treated as received
6 or accrued on the last business day referred to
7 in paragraph (1).

8 (B) Any loss resulting from an election
9 under paragraph (1) shall not be allowed for
10 any taxable year.

11 (3) ELECTION.—An election under paragraph
12 (1) shall be made in such manner as the Secretary
13 may prescribe and shall specify the readily tradable
14 securities for which such election is made. Such an
15 election, once made with respect to any readily
16 tradable security, shall be irrevocable.

17 (4) READILY TRADABLE SECURITY.—For pur-
18 poses of this subsection, the term “readily tradable
19 security” means any stock or other security which,
20 as of January 1, 1997, is readily tradable on an es-
21 tablished securities market or otherwise.

22 **SEC. 4. MIDDLE INCOME SAVINGS INCENTIVES.**

23 (a) GENERAL RULE.—Part III of subchapter B of
24 chapter 1 of the Internal Revenue Code of 1986 (relating
25 to items specifically excluded from gross income) is

1 amended by inserting after section 115 the following new
2 section:

3 **“SEC. 116. MIDDLE INCOME EXCLUSION FOR INVESTMENT**
4 **INCOME.**

5 “(a) GENERAL RULE.—In the case of an eligible indi-
6 vidual, gross income does not include qualified investment
7 income.

8 “(b) LIMITATION.—

9 “(1) IN GENERAL.—The amount excluded from
10 gross income under subsection (a) for any taxable
11 year shall not exceed \$500 (\$1,000 in the case of a
12 joint return).

13 “(2) PHASEOUT.—If the modified adjusted
14 gross income of the individuals exceeds \$40,000
15 (\$20,000 in the case of a separate return by a mar-
16 ried individual), the amount determined under para-
17 graph (1) shall be reduced by an amount equal to
18 10 percent of such excess.

19 “(c) DEFINITIONS.—For purposes of this section:

20 “(1) QUALIFIED INDIVIDUAL.—The term ‘quali-
21 fied individual’ means any individual if—

22 “(A) such individual’s modified adjusted
23 gross income for the taxable year does not ex-
24 ceed \$50,000 (\$25,000 in the case of a separate
25 return by a married individual), and

1 “(B) at least 50 percent of such individ-
2 uals modified adjusted gross income for the tax-
3 able year is attributable to earned income (as
4 defined in section 911(d)(2)).

5 For purposes of this section, marital status shall be
6 determined under section 7703.

7 “(2) QUALIFIED INVESTMENT INCOME.—The
8 term ‘qualified investment income’ means gross in-
9 come from property held for investment except that
10 such term shall not include—

11 “(A) any gain on the sale or other disposi-
12 tion of property held for investment, and

13 “(B) any income taken into account under
14 section 469 in computing income or loss from
15 a passive activity.

16 “(3) MODIFIED ADJUSTED GROSS INCOME.—
17 The term ‘modified adjusted gross income’ means
18 adjusted gross income determined—

19 “(A) without regard to this section and
20 sections 135, 911, 931, and 933, and

21 “(B) after the application of sections 86,
22 469, and 219.

23 “(d) SPECIAL RULE.—This section shall not apply in
24 the case of an estate or trust.”

1 (b) MINIMUM TAX.—Subsection (b) of section 56 of
2 such Code is amended by adding at the end thereof the
3 following new paragraph:

4 “(4) MIDDLE EXCLUSION ALLOWED.—The ex-
5 clusion provided by section 116 shall be allowed.”

6 (c) CONFORMING AMENDMENTS.—

7 (1) Subparagraph (A) of section 86(b)(2) of
8 such Code is amended by inserting “116,” before
9 “135”.

10 (2) Subparagraph (A) of section 135(c)(4) of
11 such Code is amended by inserting “116,” before
12 “911”.

13 (3) Clause (ii) of section 469(i)(3)(E) if such
14 Code is amended by striking “section 135” and in-
15 serting “sections 116 and 135”.

16 (4) Clause (ii) of section 219(g)(3)(A) of such
17 Code is amended by striking “section 135” and in-
18 serting “sections 116, 135,”.

19 (d) CLERICAL AMENDMENT.—The table of sections
20 for part III of subchapter B of chapter 1 of such Code
21 is amended by inserting after the item relating to section
22 115 the following new item:

“Sec. 116. Middle income exclusion for investment income.”

23 (e) EFFECTIVE DATE.—The amendments made by
24 this section shall apply to taxable years beginning after
25 December 31, 1993.



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