

104TH CONGRESS
1ST SESSION

H. R. 512

To amend the Internal Revenue Code of 1986 to reduce the capital gains tax on stock of domestic corporations engaged in manufacturing and to index the basis of such stock for inflation.

IN THE HOUSE OF REPRESENTATIVES

JANUARY 13, 1995

Mr. MEEHAN (for himself, Mr. FRANKS of New Jersey, and Mr. QUINN) 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 capital gains tax on stock of domestic corporations engaged in manufacturing and to index the basis of such stock for inflation.

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. REDUCTION IN INDIVIDUAL CAPITAL GAINS**
4 **RATE ON STOCK OF DOMESTIC MANUFAC-**
5 **TURERS.**

6 (a) GENERAL RULE.—Subsection (h) of section 1 of
7 the Internal Revenue Code of 1986 (relating to maximum
8 capital gains rate) is amended to read as follows:

1 “(h) MAXIMUM CAPITAL GAINS RATE.—

2 “(1) IN GENERAL.—If a taxpayer has a net
3 capital gain for any taxable year, then the tax im-
4 posed by this section shall not exceed the sum of—

5 “(A) a tax computed at the rates and in
6 the same manner as if this subsection had not
7 been enacted on the taxable income reduced by
8 the net capital gain,

9 “(B) 19 percent of the lesser of—

10 “(i) the 6-year qualified gain for the
11 taxable year, or

12 “(ii) the portion of the taxpayer’s tax-
13 able income for the taxable year which
14 would be taxed at a rate in excess of 15
15 percent (determined without regard to this
16 subsection),

17 “(C) the 23.5 percent of the lesser of—

18 “(i) the 3-year qualified gain for the
19 taxable year, or

20 “(ii) the excess of the amount de-
21 scribed in subparagraph (B)(ii) for the tax-
22 able year over the 6-year qualified gain for
23 such taxable year, and

24 “(D) 28 percent of the excess (if any) of
25 the net capital gain for the taxable year over

1 the sum of the amounts taken into account
2 under subparagraphs (B) and (C).

3 “(2) 3-YEAR QUALIFIED GAIN.—For purposes
4 of this subsection, the term ‘3-year qualified gain’
5 means the lesser of—

6 “(A) the net capital gain for the taxable
7 year, or

8 “(B) the net capital gain for the taxable
9 year determined by taking into account only
10 gain or loss from the sale or exchange of quali-
11 fied manufacturer’s stock with a post-1994
12 holding period of at least 3 years but less than
13 6 years.

14 “(3) 6-YEAR QUALIFIED GAIN.—For purposes
15 of this subsection, the term ‘6-year qualified gain’
16 means the lesser of—

17 “(A) the excess of the net capital gain for
18 the taxable year over 3-year qualified gain, or

19 “(B) the net capital gain for the taxable
20 year determined by taking into account only
21 gain or loss from the sale or exchange of quali-
22 fied manufacturer’s stock with a post-1994
23 holding period of at least 6 years.

24 “(4) QUALIFIED MANUFACTURER’S STOCK.—
25 For purposes of this subsection, the term ‘qualified

1 manufacturer's stock' means stock of any domestic
2 C corporation if any trade or business of such cor-
3 poration is described in any 2-digit Standard Indus-
4 trial Classification Code relating to manufacturing.

5 “(5) POST-1994 HOLDING PERIOD.—For pur-
6 poses of this subsection, the term ‘post-1994 holding
7 period’ means the portion of the holding period after
8 December 31, 1994.

9 “(6) TREATMENT OF PASS-THRU ENTITIES.—

10 “(A) IN GENERAL.—In applying this sub-
11 section with respect to any pass-thru entity, the
12 determination of the period for which any gain
13 or loss is properly taken into account shall be
14 made at the entity level.

15 “(B) PASS-THRU ENTITY.—For purposes
16 of subparagraph (A), the term ‘pass-thru entity’
17 means—

18 “(i) a regulated investment company,

19 “(ii) a real estate investment trust,

20 “(iii) an S corporation,

21 “(iv) a partnership,

22 “(v) an estate or trust, and

23 “(vi) a common trust fund.”

24 (b) TECHNICAL AMENDMENTS.—

1 (1)(A) Section 170(e)(1)(B) of such Code is
2 amended by inserting “the applicable percentage of”
3 before “the amount of gain”.

4 (B) Section 170(e)(1) of such Code is amended
5 by adding at the end the following new sentence:
6 “For purposes of subparagraph (B), the term ‘appli-
7 cable percentage’ means the percentage determined
8 by dividing the rate of tax imposed by section 1(h)
9 by 28, or, in the case of a corporation, the rate of
10 tax imposed by section 1201(a) by 35.”

11 (2)(A) The second sentence of section
12 7518(g)(6)(A) of such Code is amended by striking
13 “28 percent (34 percent in the case of a corpora-
14 tion)” and inserting “the rate of tax determined
15 under such section”.

16 (B) The second sentence of section
17 607(h)(6)(A) of the Merchant Marine Act, 1936, is
18 amended by striking “28 percent (34 percent in the
19 case of a corporation)” and inserting “the rate of
20 tax determined under such section”.

21 **SEC. 2. REDUCTION IN CORPORATE CAPITAL GAINS RATE**
22 **ON STOCK OF DOMESTIC MANUFACTURERS.**

23 (a) GENERAL RULE.—Section 1201 of the Internal
24 Revenue Code of 1986 (relating to alternative tax for cor-
25 porations) is amended by redesignating subsection (b) as

1 subsection (c) and by striking subsection (a) and inserting
2 the following:

3 “(a) GENERAL RULE.—If for any taxable year a cor-
4 poration has a net capital gain, then, in lieu of the tax
5 imposed by section 11, 511, or 831(a) (whichever applies),
6 there is hereby imposed a tax (if such tax is less than
7 the tax imposed by such section) which shall consist of
8 the sum of—

9 “(1) a tax computed on the taxable income re-
10 duced by the net capital gain, at the same rates and
11 in the same manner as if this subsection had not
12 been enacted,

13 “(2) 19 percent of the lesser of—

14 “(A) the 6-year qualified gain for the tax-
15 able year, or

16 “(B) the portion of the taxpayer’s taxable
17 income for the taxable year which would be
18 taxed at a rate in excess of 15 percent (deter-
19 mined without regard to this subsection),

20 “(3) 23.5 percent of the lesser of—

21 “(A) the 3-year qualified gain for the tax-
22 able year, or

23 “(B) the excess of the amount described in
24 paragraph (2)(B) for the taxable year over the
25 6-year qualified gain for such taxable year, and

1 basis rules of general application) is amended by inserting
2 after section 1021 the following new section:

3 **“SEC. 1022. INDEXING OF QUALIFIED MANUFACTURER’S**
4 **STOCK FOR PURPOSES OF DETERMINING**
5 **GAIN OR LOSS.**

6 “(a) GENERAL RULE.—Except as otherwise provided
7 in this subsection, if any qualified manufacturer’s stock
8 which has been held for more than 3 years (taking into
9 account only the portion of the holding period after De-
10 cember 31, 1994) is sold or otherwise disposed of, for pur-
11 poses of this title the indexed basis of the stock shall be
12 substituted for its adjusted basis.

13 “(b) QUALIFIED MANUFACTURER’S STOCK.—For
14 purposes of this section, the term ‘qualified manufactur-
15 er’s stock’ means stock of any domestic C corporation if—

16 “(1) any trade or business of such corporation
17 is described in any 2-digit Standard Industrial Clas-
18 sification Code relating to manufacturing, and

19 “(2) such stock is a capital asset in the hands
20 of the taxpayer.

21 “(c) INDEXED BASIS.—For purposes of this sec-
22 tion—

23 “(1) GENERAL RULE.—The indexed basis for
24 any stock is—

1 “(A) the adjusted basis of the stock, multi-
2 plied by

3 “(B) the applicable inflation ratio.

4 “(2) APPLICABLE INFLATION RATIO.—The ap-
5 plicable inflation ratio for any stock is the percent-
6 age arrived at by dividing—

7 “(A) the gross domestic product deflator
8 for the calendar quarter in which the disposi-
9 tion takes place, by

10 “(B) the gross domestic product deflator
11 for the calendar quarter in which the stock was
12 acquired by the taxpayer (or, if later, the cal-
13 endar quarter ending on December 31, 1994).

14 The applicable inflation ratio shall never be less than
15 1. The applicable inflation ratio for any stock shall
16 be rounded to the nearest $\frac{1}{1000}$.

17 “(3) GROSS DOMESTIC PRODUCT DEFLATOR.—
18 The gross domestic product deflator for any cal-
19 endar quarter is the implicit price deflator for the
20 gross domestic product for such quarter (as shown
21 in the first revision thereof).

22 “(d) TREATMENT OF REGULATED INVESTMENT
23 COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

24 “(1) ADJUSTMENTS AT ENTITY LEVEL.—

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

7 “(B) EXCEPTION FOR QUALIFICATION
8 PURPOSES.—This section shall not apply for
9 purposes of sections 851(b) and 856(c).

10 “(2) ADJUSTMENTS TO INTERESTS HELD IN
11 ENTITY.—

12 “(A) IN GENERAL.—Stock in a qualified
13 investment entity shall be qualified manufactur-
14 er’s stock for any calendar month in the same
15 ratio as the fair market value of the qualified
16 manufacturer’s stock held by such entity at the
17 close of such month bears to the fair market
18 value of all assets of such entity at the close of
19 such month.

20 “(B) RATIO OF 90 PERCENT OR MORE.—If
21 the ratio for any calendar month determined
22 under subparagraph (A) would (but for this
23 subparagraph) be 90 percent or more, such
24 ratio for such month shall be 100 percent.

1 “(C) RATIO OF 10 PERCENT OR LESS.—If
2 the ratio for any calendar month determined
3 under subparagraph (A) would (but for this
4 subparagraph) be 10 percent or less, such ratio
5 for such month shall be zero.

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

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

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

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

23 “(e) OTHER PASS-THRU ENTITIES.—

24 “(1) PARTNERSHIPS.—In the case of a partner-
25 ship, the adjustment made under subsection (a) at

1 the partnership level shall be passed through to the
2 partners.

3 “(2) S CORPORATIONS.—In the case of an S
4 corporation, the adjustment made under subsection
5 (a) at the corporate level shall be passed through to
6 the shareholders.

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.

11 “(f) DISPOSITIONS BETWEEN RELATED PERSONS.—

12 “(1) IN GENERAL.—This section shall not apply
13 to any sale or other disposition of property between
14 related persons except to the extent that the basis
15 of such property in the hands of the transferee is a
16 substituted basis.

17 “(2) RELATED PERSONS DEFINED.—For pur-
18 poses of this section, the term ‘related persons’
19 means—

20 “(A) persons bearing a relationship set
21 forth in section 267(b), and

22 “(B) persons treated as single employer
23 under subsection (b) or (c) of section 414.

24 “(g) TRANSFERS TO INCREASE INDEXING ADJUST-
25 MENT.—If any person transfers cash, debt, or any other

1 property to another person and the principal purpose of
2 such transfer is to secure or increase an adjustment under
3 subsection (a), the Secretary may disallow part or all of
4 such adjustment or increase.

5 “(h) SPECIAL RULES.—For purposes of this section:

6 “(1) TREATMENT AS SEPARATE STOCK.—A
7 substantial contribution to capital of a corporation
8 shall be treated as separate stock in such corpora-
9 tion.

10 “(2) STOCK WHICH IS NOT QUALIFIED MANU-
11 FACTURER’S STOCK THROUGHOUT HOLDING PE-
12 RIOD.—The applicable inflation ratio shall be appro-
13 priately reduced for periods during which stock is
14 not qualified manufacturer’s stock.

15 “(3) TREATMENT OF CERTAIN DISTRIBU-
16 TIONS.—A distribution with respect to stock in a
17 corporation which is not a dividend shall be treated
18 as a disposition.

19 “(4) ACQUISITION DATE WHERE THERE HAS
20 BEEN PRIOR APPLICATION OF SUBSECTION (a)(1)
21 WITH RESPECT TO THE TAXPAYER.—If there has
22 been a prior application of subsection (a) to stock
23 while such stock was held by the taxpayer, the date
24 of acquisition of such stock by the taxpayer shall be

1 treated as not earlier than the date of the most re-
2 cent such prior application.

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

6 (b) CLERICAL AMENDMENT.—The table of sections
7 for part II of subchapter O of chapter 1 of such Code
8 is amended by inserting after the item relating to section
9 1021 the following new item:

“Sec. 1022. Indexing of qualified manufacturer’s stock for pur-
poses of determining gain or loss.”

10 (c) ADJUSTMENT TO APPLY FOR PURPOSES OF DE-
11 TERMINING EARNINGS AND PROFITS.—Subsection (f) of
12 section 312 of such Code (relating to effect on earnings
13 and profits of gain or loss and of receipt of tax-free dis-
14 tributions) is amended by adding at the end thereof the
15 following new paragraph:

16 “(3) EFFECT ON EARNINGS AND PROFITS OF
17 INDEXED BASIS.—

**For substitution of indexed basis for adjusted
basis in the case of the disposition of qualified man-
ufacturer’s stock, see section 1022(a).”**

18 **SEC. 4. EFFECTIVE DATE.**

19 The amendments made by this Act shall apply to tax-
20 able years beginning after December 31, 1994.

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