

104<sup>TH</sup> CONGRESS  
1<sup>ST</sup> SESSION

# H. R. 537

To amend the Internal Revenue Code of 1986 to index the basis of certain assets acquired on or after January 1, 1995, for purposes of determining gain, and for other purposes.

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## IN THE HOUSE OF REPRESENTATIVES

JANUARY 17, 1995

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

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## A BILL

To amend the Internal Revenue Code of 1986 to index the basis of certain assets acquired on or after January 1, 1995, for purposes of determining gain, 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. INDEXING OF CERTAIN ASSETS ACQUIRED ON**  
4 **OR AFTER JANUARY 1, 1995, FOR PURPOSES**  
5 **OF DETERMINING GAIN.**

6 (a) IN GENERAL.—Part II of subchapter O of chap-  
7 ter 1 of the Internal Revenue Code of 1986 (relating to

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

3 **“SEC. 1022. INDEXING OF CERTAIN ASSETS ACQUIRED ON**  
4 **OR AFTER JANUARY 1, 1995, FOR PURPOSES**  
5 **OF DETERMINING GAIN.**

6 “(a) GENERAL RULE.—

7 “(1) INDEXED BASIS SUBSTITUTED FOR AD-  
8 JUSTED BASIS.—Solely for purposes of determining  
9 gain on the sale or other disposition by a taxpayer  
10 (other than a corporation) of an indexed asset which  
11 has been held for more than 1 year, the indexed  
12 basis of the asset shall be substituted for its ad-  
13 justed basis.

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

15 “(A) IN GENERAL.—Paragraph (1) shall  
16 not apply for purposes of determining the  
17 amount of recapture gain on the sale or other  
18 disposition of an indexed asset, but the amount  
19 of any such recapture gain shall increase the  
20 adjusted basis of the asset for purposes of ap-  
21 plying paragraph (1) to determine the amount  
22 of other gain on such sale or other disposition.

23 “(B) RECAPTURE GAIN.—For purposes of  
24 subparagraph (A), the term ‘recapture gain’

1 means any gain treated as ordinary income  
2 under section 1245, 1250, or 1254.

3 “(b) INDEXED ASSET.—

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

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

7 “(B) any tangible property (or any interest  
8 therein),

9 which is a capital asset or property used in the trade  
10 or business (as defined in section 1231(b)) and the  
11 holding period of which begins on or after January  
12 1, 1995.

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

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

19 “(B) COLLECTIBLES.—Any collectible (as  
20 defined in section 408(m)(2) without regard to  
21 section 408(m)(3)).

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

1           “(D) NET LEASE PROPERTY.—In the case  
2 of a lessor, net lease property (within the mean-  
3 ing of subsection (1)(3)).

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

6           “(F) STOCK IN S CORPORATIONS.—Stock  
7 in an S corporation.

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

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

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

24           “(c) INDEXED BASIS.—For purposes of this sec-  
25 tion—

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

3           “(A) the adjusted basis of the asset, multi-  
4 plied by

5           “(B) the applicable inflation ratio.

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

9           “(A) The CPI for the calendar year pre-  
10 ceding the calendar year in which the disposi-  
11 tion takes place, by

12           “(B) the CPI for the calendar year preced-  
13 ing the calendar year in which the taxpayer’s  
14 holding period for such asset began.

15 The applicable inflation ratio shall not be taken into  
16 account unless it is greater than 1. The applicable  
17 inflation ratio for any asset shall be rounded to the  
18 nearest one-thousandth.

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

22           “(A) such disposition shall be treated as  
23 occurring on the last day of such calendar year,  
24 and

1           “(B) the taxpayer’s holding period for such  
2           asset shall be treated as beginning in the same  
3           calendar year as would be determined for an  
4           asset actually disposed of on such last day with  
5           a holding period of the same length as the ac-  
6           tual holding period of the asset involved.

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

10          “(d) SHORT SALES.—

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

22           “(2) SHORT SALE OF SUBSTANTIALLY IDEN-  
23           TICAL PROPERTY.—If the taxpayer or the taxpayer’s  
24           spouse sells short property substantially identical to  
25           an asset held by the taxpayer, the asset held by the

1 taxpayer and the substantially identical property  
2 shall not be treated as indexed assets for the short  
3 sale period.

4 “(3) SHORT SALE PERIOD.—For purposes of  
5 this subsection, the short sale period begins on the  
6 day after property is sold and ends on the closing  
7 date for the sale.

8 “(e) TREATMENT OF REGULATED INVESTMENT  
9 COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

10 “(1) ADJUSTMENTS AT ENTITY LEVEL.—

11 “(A) IN GENERAL.—Except as otherwise  
12 provided in this paragraph, the adjustment  
13 under subsection (a) shall be allowed to any  
14 qualified investment entity (including for pur-  
15 poses of determining the earnings and profits of  
16 such entity).

17 “(B) EXCEPTION FOR CORPORATE SHARE-  
18 HOLDERS.—Under regulations—

19 “(i) in the case of a distribution by a  
20 qualified investment entity (directly or in-  
21 directly) to a corporation—

22 “(I) the determination of whether  
23 such distribution is a dividend shall be  
24 made without regard to this section,  
25 and

1           “(II) the amount treated as gain  
2           by reason of the receipt of any capital  
3           gain dividend shall be increased by the  
4           percentage by which the entity’s net  
5           capital gain for the taxable year deter-  
6           mined without regard to this section  
7           exceeds the entity’s net capital gain  
8           for such year determined with regard  
9           to this section, and

10           “(ii) there shall be other appropriate  
11           adjustments (including deemed distribu-  
12           tions) so as to ensure that the benefits of  
13           this section are not allowed (directly or in-  
14           directly) to corporate shareholders of quali-  
15           fied investment entities.

16           For purposes of the preceding sentence, any  
17           amount includible in gross income under section  
18           852(b)(3)(D) shall be treated as a capital gain  
19           dividend and an S corporation shall not be  
20           treated as a corporation.

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

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

1           “(i) TAX ON FAILURE TO DISTRIBUTE  
2 ENTIRE GAIN.—If any amount is subject to  
3 tax under section 852(b)(3)(A) for any  
4 taxable year, the amount on which tax is  
5 imposed under such section shall be in-  
6 creased by the percentage determined  
7 under subparagraph (B)(i)(II). A similar  
8 rule shall apply in the case of any amount  
9 subject to tax under paragraph (2) or (3)  
10 of section 857(b) to the extent attributable  
11 to the excess of the net capital gain over  
12 the deduction for dividends paid deter-  
13 mined with reference to capital gain divi-  
14 dends only. The first sentence of this  
15 clause shall not apply to so much of the  
16 amount subject to tax under section  
17 852(b)(3)(A) as is designated by the com-  
18 pany under section 852(b)(3)(D).

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

23           “(2) ADJUSTMENTS TO INTERESTS HELD IN  
24 ENTITY.—

1           “(A) IN GENERAL.—Stock in a qualified  
2 investment entity shall be an indexed asset for  
3 any calendar month in the same ratio as the  
4 fair market value of the assets held by such en-  
5 tity at the close of such month which are in-  
6 dexed assets (determined without regard to the  
7 requirement that the holding period begin on or  
8 after January 1, 1995) bears to the fair market  
9 value of all assets of such entity at the close of  
10 such month.

11           “(B) RATIO OF 90 PERCENT OR MORE.—If  
12 the ratio for any calendar month determined  
13 under subparagraph (A) would (but for this  
14 subparagraph) be 90 percent or more, such  
15 ratio for such month shall be 100 percent.

16           “(C) RATIO OF 10 PERCENT OR LESS.—If  
17 the ratio for any calendar month determined  
18 under subparagraph (A) would (but for this  
19 subparagraph) be 10 percent or less, such ratio  
20 for such month shall be zero.

21           “(D) VALUATION OF ASSETS IN CASE OF  
22 REAL ESTATE INVESTMENT TRUSTS.—Nothing  
23 in this paragraph shall require a real estate in-  
24 vestment trust to value its assets more fre-  
25 quently than once each 36 months (except

1 where such trust ceases to exist). The ratio  
2 under subparagraph (A) for any calendar  
3 month for which there is no valuation shall be  
4 the trustee's good faith judgment as to such  
5 valuation.

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

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

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

13 “(f) OTHER PASS-THRU ENTITIES.—

14 “(1) PARTNERSHIPS.—In the case of a partner-  
15 ship, the adjustment made under subsection (a) at  
16 the partnership level shall be passed through to the  
17 partners (but only for purposes of determining the  
18 income of partners who are not corporations).

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

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

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

13          “(h) TRANSFERS TO INCREASE INDEXING ADJUST-  
14          MENT.—If any person transfers cash, debt, or any other  
15          property to another person and the principal purpose of  
16          such transfer is to secure or increase an adjustment under  
17          subsection (a), the Secretary may disallow part or all of  
18          such adjustment or increase.

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

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

23                          “(A) A substantial improvement to prop-  
24                          erty.

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

3           “(C) Any other portion of an asset to the  
4           extent that separate treatment of such portion  
5           is appropriate to carry out the purposes of this  
6           section.

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

11          “(3) NET LEASE PROPERTY DEFINED.—The  
12          term ‘net lease property’ means leased property  
13          where—

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

17                 “(B) for the period of the lease, the sum  
18                 of the deductions with respect to such property  
19                 which are allowable to the lessor solely by rea-  
20                 son of section 162 (other than rents and reim-  
21                 bursed amounts with respect to such property)  
22                 is 15 percent or less of the rental income pro-  
23                 duced by such property.

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

4       (b) GAINS AND LOSSES FROM INDEXED ASSETS NOT  
5 TAKEN INTO ACCOUNT UNDER LIMITATION ON INVEST-  
6 MENT INTEREST.—Subparagraph (B) of section  
7 163(d)(4) of such Code (defining investment income) is  
8 amended by adding at the end thereof the following new  
9 sentences: “Gain from the sale or other disposition of an  
10 indexed asset (as defined in section 1022) held for more  
11 than 1 year shall not be taken into account for purposes  
12 of the preceding sentence. The preceding sentence shall  
13 not apply to gain from the sale or other disposition of any  
14 such asset if the taxpayer elects to waive the benefits of  
15 section 1022 in determining the amount of such gain.”

16       (c) RECAPTURE OF ENTIRE AMOUNT OF DEPRECIA-  
17 TION UNDER SECTION 1250.—Section 1250 of such Code  
18 (relating to gain from dispositions of certain depreciable  
19 realty) is amended by adding at the end thereof the follow-  
20 ing new subsection:

21       “(i) RECAPTURE OF ENTIRE AMOUNT OF DEPRECIA-  
22 TION IN CASE OF PROPERTY TO WHICH SECTION 1022  
23 APPLIES.—

24               “(1) IN GENERAL.—In the case of any taxpayer  
25       other than a corporation—

1           “(A) subsection (a) shall be applied with  
2           respect to any disposition of section 1250 prop-  
3           erty to which section 1022 applies as if it read  
4           as follows:

5           “(a) GENERAL RULE.—Except as otherwise pro-  
6           vided in this section, if section 1250 property is disposed  
7           of, the lesser of—

8           “(1) the depreciation adjustments in respect of  
9           such property, or

10          “(2) the excess of—

11           “(A) the amount realized (or, in the case  
12           of a disposition other than sale, exchange, or in-  
13           voluntary conversion, the fair market value of  
14           such property), over

15           “(B) the adjusted basis of such property,  
16           shall be treated as gain which is ordinary income. Such  
17           gain shall be recognized notwithstanding any other provi-  
18           sion of this subtitle.’, and

19           “(B) in the case of any disposition de-  
20           scribed in subparagraph (A), subsections (e)  
21           and (f) shall not apply and appropriate adjust-  
22           ments shall be made in the provisions of sub-  
23           section (d).

1           “(2) SPECIAL RULES FOR CERTAIN ENTITIES.—  
2           For purposes of paragraph (1), the following shall  
3           not be treated as a corporation:

4                   “(A) An S corporation.

5                   “(B) A regulated investment company.

6                   “(C) A real estate investment trust.

7           “(3) COORDINATION WITH SECTION 453(i).—  
8           Subsection (i) of section 453 shall be applied with-  
9           out regard to this subsection.”.

10          (d) CLERICAL AMENDMENT.—The table of sections  
11 for part II of subchapter O of chapter 1 of such Code  
12 is amended by inserting after the item relating to section  
13 1021 the following new item:

                  “Sec. 1022. Indexing of certain assets acquired on or after Janu-  
                  ary 1, 1995, for purposes of determining gain.”.

14          (e) EFFECTIVE DATE.—

15               (1) IN GENERAL.—The amendments made by  
16 this section shall apply to the disposition of any  
17 property the holding period of which begins on or  
18 after January 1, 1995.

19               (2) CERTAIN TRANSACTIONS BETWEEN RELAT-  
20 ED PERSONS.—The amendments made by this sec-  
21 tion shall not apply to the disposition of any prop-  
22 erty acquired on or after January 1, 1995, from a  
23 related person (as defined in section 465(b)(3)(C) of  
24 the Internal Revenue Code of 1986) if—

1 (A) such property was so acquired for a  
2 price less than the property's fair market value,  
3 and

4 (B) the amendments made by this section  
5 did not apply to such property in the hands of  
6 such related person.

7 (f) ELECTION TO RECOGNIZE GAIN ON READILY  
8 TRADEABLE SECURITIES HELD ON JANUARY 1, 1995.—

9 (1) IN GENERAL.—If a taxpayer other than a  
10 corporation holds any readily tradable security on  
11 January 1, 1995, the taxpayer may elect to treat  
12 such security as having been sold on the last busi-  
13 ness day before such date for an amount equal to its  
14 closing market price on such last business day (and  
15 as having been reacquired on such last business day  
16 for an amount equal to such closing market price).

17 (2) TREATMENT OF GAIN OR LOSS.—

18 (A) Any gain resulting from an election  
19 under paragraph (1) shall be treated as received  
20 or accrued on the last business day referred to  
21 in paragraph (1).

22 (B) Any loss resulting from an election  
23 under paragraph (1) shall not be allowed for  
24 any taxable year.

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

7           (4) READILY TRADABLE SECURITY.—For pur-  
8           poses of this subsection, the term “readily tradable  
9           security” means any stock or other security which,  
10          as of January 1, 1995, is readily tradable on an es-  
11          tablished securities market or otherwise.

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