

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

# H. R. 56

To amend the Internal Revenue Code of 1986 to provide all taxpayers with a 50 percent deduction for capital gains, to index the basis of certain capital assets, and to allow the capital loss deduction for losses on the sale or exchange of an individual's principal residence.

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## IN THE HOUSE OF REPRESENTATIVES

JANUARY 4, 1995

Mr. ARCHER (for himself, Mr. ZIMMER, Mr. CRANE, Mr. THOMAS, Mr. SHAW, Mrs. JOHNSON of Connecticut, Mr. BUNNING of Kentucky, Mr. HOUGHTON, Mr. HERGER, Mr. MCCRERY, Mr. HANCOCK, Mr. CAMP, Mr. RAMSTAD, Mr. NUSSLE, Mr. SAM JOHNSON of Texas, Ms. DUNN of Washington, Mr. COLLINS of Georgia, Mr. PORTMAN, Mr. ENGLISH of Pennsylvania, Mr. ENSIGN, Mr. CHRISTENSEN, Mr. BLILEY, Mr. EMERSON, Mr. GREENWOOD, Mr. CANADY, Mr. LATHAM, Mr. BURTON of Indiana, Mrs. MEYERS of Kansas, Mr. SAXTON, Mr. MCINTOSH, Mr. ROYCE, Mr. LIVINGSTON, Mr. FRISA, Mr. STUMP, Mr. TAYLOR of North Carolina, Mr. BARTLETT of Maryland, Mr. HUTCHINSON, Mr. BAKER of California, Mr. CUNNINGHAM, Mr. QUILLEN, Mr. ALLARD, Mr. SMITH of Texas, Mr. ROHRABACHER, Mr. BACHUS, Ms. PRYCE, Mr. BLUTE, Mr. FORBES, Mr. GALLEGLY, Mr. DORNAN, Mr. COX, and Mr. LEACH) 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 provide all taxpayers with a 50 percent deduction for capital gains, to index the basis of certain capital assets, and to allow the capital loss deduction for losses on the sale or exchange of an individual's principal residence.

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 “Capital Formation and  
5 Jobs Creation Act of 1995”.

6 **SEC. 2. 50 PERCENT CAPITAL GAINS DEDUCTION.**

7        (a) GENERAL RULE.—Part I of subchapter P of  
8 chapter 1 of the Internal Revenue Code of 1986 (relating  
9 to treatment of capital gains) is amended to read as  
10 follows:

11        **“PART I—TREATMENT OF CAPITAL GAINS**

“Sec. 1201. Capital gains deduction.

12 **“SEC. 1201. CAPITAL GAINS DEDUCTION.**

13        “(a) GENERAL RULE.—If for any taxable year a tax-  
14 payer has a net capital gain, 50 percent of such gain shall  
15 be a deduction from gross income.

16        “(b) ESTATES AND TRUSTS.—In the case of an es-  
17 tate or trust, the deduction shall be computed by excluding  
18 the portion (if any) of the gains for the taxable year from  
19 sales or exchanges of capital assets which, under sections  
20 652 and 662 (relating to inclusions of amounts in gross  
21 income of beneficiaries of trusts), is includible by the in-  
22 come beneficiaries as gain derived from the sale or ex-  
23 change of capital assets.

1       “(c) COORDINATION WITH TREATMENT OF CAPITAL  
2 GAIN UNDER LIMITATION ON INVESTMENT INTEREST.—

3 For purposes of this section, the net capital gain for any  
4 taxable year shall be reduced (but not below zero) by the  
5 amount which the taxpayer takes into account as invest-  
6 ment income under section 163(d)(4)(B)(iii).

7       “(d) TRANSITIONAL RULE.—

8           “(1) IN GENERAL.—In the case of a taxable  
9 year which includes January 1, 1995—

10               “(A) the amount taken into account as the  
11 net capital gain under subsection (a) shall not  
12 exceed the net capital gain determined by only  
13 taking into account gains and losses properly  
14 taken into account for the portion of the tax-  
15 able year on or after January 1, 1995, and

16               “(B) if the net capital gain for such year  
17 exceeds the amount taken into account under  
18 subsection (a), the rate of tax imposed by sec-  
19 tion 1 on such excess shall not exceed 28 per-  
20 cent.

21       “(2) SPECIAL RULES FOR PASS-THRU ENTI-  
22 TIES.—

23           “(A) IN GENERAL.—In applying paragraph  
24 (1) with respect to any pass-thru entity, the de-  
25 termination of when gains and losses are prop-

1           erly taken into account shall be made at the en-  
2           tity level.

3           “(B) PASS-THRU ENTITY DEFINED.—For  
4           purposes of subparagraph (A), the term ‘pass-  
5           thru entity’ means—

6                     “(i) a regulated investment company,

7                     “(ii) a real estate investment trust,

8                     “(iii) an S corporation,

9                     “(iv) a partnership,

10                    “(v) an estate or trust, and

11                    “(vi) a common trust fund.”

12           (b) DEDUCTION ALLOWABLE IN COMPUTING AD-  
13 JUSTED GROSS INCOME.—Subsection (a) of section 62 of  
14 such Code is amended by inserting after paragraph (15)  
15 the following new paragraph:

16                    “(16) LONG-TERM CAPITAL GAINS.—The de-  
17                    duction allowed by section 1201.”

18           (c) TECHNICAL AND CONFORMING CHANGES.—

19                    (1) Section 13113 of the Revenue Reconcili-  
20                    ation Act of 1993 (relating to 50-percent exclusion  
21                    for gain from certain small business stock), and the  
22                    amendments made by such section, are hereby re-  
23                    pealed; and the Internal Revenue Code of 1986 shall  
24                    be applied as if such section (and amendments) had  
25                    never been enacted.

1           (2) Section 1 of such Code is amended by strik-  
2           ing subsection (h).

3           (3) Paragraph (1) of section 170(e) of such  
4           Code is amended by striking “the amount of gain”  
5           in the material following subparagraph (B)(ii) and  
6           inserting “50 percent of the amount of gain”.

7           (4)(A) Paragraph (2) of section 172(d) of such  
8           Code is amended to read as follows:

9           “(2) CAPITAL GAINS AND LOSSES.—

10           “(A) LOSSES OF TAXPAYERS OTHER THAN  
11           CORPORATIONS.—In the case of a taxpayer  
12           other than a corporation, the amount deductible  
13           on account of losses from sales or exchanges of  
14           capital assets shall not exceed the amount in-  
15           cludible on account of gains from sales or ex-  
16           changes of capital assets.

17           “(B) DEDUCTION UNDER SECTION 1201.—  
18           The deduction under section 1201 shall not be  
19           allowed.”

20           (B) Subparagraph (B) of section 172(d)(4) of  
21           such Code is amended by striking “paragraphs (1)  
22           and (3)” and inserting “paragraphs (1), (2)(B), and  
23           (3)”.

24           (5) Paragraph (4) of section 642(c) of such  
25           Code is amended to read as follows:

1           “(4) ADJUSTMENTS.—To the extent that the  
2 amount otherwise allowable as a deduction under  
3 this subsection consists of gain from the sale or ex-  
4 change of capital assets held for more than 1 year,  
5 proper adjustment shall be made for any deduction  
6 allowable to the estate or trust under section 1201  
7 (relating to deduction for excess of capital gains over  
8 capital losses). In the case of a trust, the deduction  
9 allowed by this subsection shall be subject to section  
10 681 (relating to unrelated business income).”

11           (6) Paragraph (3) of section 643(a) of such  
12 Code is amended by adding at the end thereof the  
13 following new sentence: “The deduction under sec-  
14 tion 1201 (relating to deduction of excess of capital  
15 gains over capital losses) shall not be taken into  
16 account.”

17           (7) Paragraph (4) of section 691(c) of such  
18 Code is amended by striking “sections 1(h), 1201,  
19 and 1211” and inserting “sections 1201 and 1211”.

20           (8) The second sentence of section 871(a)(2) of  
21 such Code is amended by inserting “such gains and  
22 losses shall be determined without regard to section  
23 1201 (relating to deduction for capital gains) and”  
24 after “except that”.

1           (9) Subsection (d) of section 1044 of such Code  
2 is amended by striking the last sentence.

3           (10)(A) Paragraph (2) of section 1211(b) of  
4 such Code is amended to read as follows:

5           “(2) the sum of—

6                 “(A) the excess of the net short-term cap-  
7 ital loss over the net long-term capital gain, and

8                 “(B) one-half of the excess of the net long-  
9 term capital loss over the net short-term capital  
10 gain.”

11           (B) So much of paragraph (2) of section  
12 1212(b) of such Code as precedes subparagraph (B)  
13 thereof is amended to read as follows:

14           “(2) SPECIAL RULES.—

15                 “(A) ADJUSTMENTS.—

16                         “(i) For purposes of determining the  
17 excess referred to in paragraph (1)(A),  
18 there shall be treated as short-term capital  
19 gain in the taxable year an amount equal  
20 to the lesser of—

21                                 “(I) the amount allowed for the  
22 taxable year under paragraph (1) or  
23 (2) of section 1211(b), or

24                                 “(II) the adjusted taxable income  
25 for such taxable year.

1           “(ii) For purposes of determining the  
2           excess referred to in paragraph (1)(B),  
3           there shall be treated as short-term capital  
4           gain in the taxable year an amount equal  
5           to the sum of—

6                   “(I) the amount allowed for the  
7                   taxable year under paragraph (1) or  
8                   (2) of section 1211(b) or the adjusted  
9                   taxable income for such taxable year,  
10                  whichever is the least, plus

11                   “(II) the excess of the amount  
12                   described in subclause (I) over the net  
13                   short-term capital loss (determined  
14                   without regard to this subsection) for  
15                   such year.”

16           (11) Paragraph (1) of section 1402(i) of such  
17           Code is amended by inserting “, and the deduction  
18           provided by section 1201 shall not apply” before the  
19           period at the end thereof.

20           (12) Section 12 of such Code is amended by  
21           striking paragraph (4) and redesignating the follow-  
22           ing paragraphs accordingly.

23           (13) Paragraph (2) of section 527(b) of such  
24           Code is hereby repealed.

1           (14) Subparagraph (D) of section 593(b)(2) of  
2 such Code is amended by adding “and” at the end  
3 of clause (iii), by striking “, and” at the end of  
4 clause (iv) and inserting a period, and by striking  
5 clause (v).

6           (15) Paragraph (2) of section 801(a) of such  
7 Code is hereby repealed.

8           (16) Subsection (c) of section 831 of such Code  
9 is amended by striking paragraph (1) and redesignating the following paragraphs accordingly.  
10

11           (17)(A) Subparagraph (A) of section 852(b)(3)  
12 of such Code is amended by striking “, determined  
13 as provided in section 1201(a), on” and inserting  
14 “of 17.5 percent of”.

15           (B) Clause (iii) of section 852(b)(3)(D) of such  
16 Code is amended—

17                 (i) by striking “65 percent” and inserting  
18 “82.5 percent”, and

19                 (ii) by striking “section 1201(a)” and inserting “subparagraph (A)”.

21           (18) Clause (ii) of section 857(b)(3)(A) of such  
22 Code is amended by striking “determined at the rate  
23 provided in section 1201(a) on” and inserting “of  
24 17.5 percent of”.

1           (19) Paragraph (1) of section 882(a) of such  
2 Code is amended by striking “section 11, 55, 59A,  
3 or 1201(a)” and inserting “section 11, 55, or 59A”.

4           (20) Subsection (b) of section 904 of such Code  
5 is amended by striking paragraphs (2)(B), (3)(B),  
6 (3)(D), and (3)(E).

7           (21) Subsection (b) of section 1374 of such  
8 Code is amended by striking paragraph (4).

9           (22) Subsection (b) of section 1381 is amended  
10 by striking “or 1201”.

11           (23) Subsection (e) of section 1445 of such  
12 Code is amended—

13                 (A) in paragraph (1) by striking “35 per-  
14 cent (or, to the extent provided in regulations,  
15 28 percent)” and inserting “17.5 percent (or, to  
16 the extent provided in regulations, 19.8 per-  
17 cent)”, and

18                 (B) in paragraph (2) by striking “35 per-  
19 cent” and inserting “17.5 percent”.

20           (24) Clause (i) of section 6425(c)(1)(A) of such  
21 Code is amended by striking “or 1201(a)”.

22           (25) Clause (i) of section 6655(g)(1)(A) of such  
23 Code is amended by striking “or 1201(a)”.

24           (26)(A) The second sentence of section  
25 7518(g)(6)(A) of such Code is amended—

1 (i) by striking “during a taxable year to  
2 which section 1(h) or 1201(a) applies”, and

3 (ii) by striking “28 percent (34 percent”  
4 and inserting “19.8 percent (17.5 percent”.

5 (B) The second sentence of section  
6 607(h)(6)(A) of the Merchant Marine Act, 1936 is  
7 amended—

8 (i) by striking “during a taxable year to  
9 which section 1(h) or 1201(a) of such Code ap-  
10 plies”, and

11 (ii) by striking “28 percent (34 percent”  
12 and inserting “19.8 percent (17.5 percent”.

13 (d) EFFECTIVE DATE.—

14 (1) IN GENERAL.—Except as otherwise pro-  
15 vided in this subsection, the amendments made by  
16 this section shall apply to taxable years ending after  
17 December 31, 1994.

18 (2) CONTRIBUTIONS.—The amendment made  
19 by subsection (c)(3) shall apply only to contributions  
20 on or after January 1, 1995.

21 (3) WITHHOLDING.—The amendment made by  
22 subsection (c)(23) shall apply only to amounts paid  
23 after the date of the enactment of this Act.

1 **SEC. 3. INDEXING OF CERTAIN ASSETS FOR PURPOSES OF**  
2 **DETERMINING GAIN OR LOSS.**

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

7 **“SEC. 1022. INDEXING OF CERTAIN ASSETS FOR PURPOSES**  
8 **OF DETERMINING GAIN OR LOSS.**

9 “(a) GENERAL RULE.—

10 “(1) INDEXED BASIS SUBSTITUTED FOR AD-  
11 JUSTED BASIS.—Except as otherwise provided in  
12 this subsection, if an indexed asset which has been  
13 held for more than 1 year is sold or otherwise dis-  
14 posed of, for purposes of this title the indexed basis  
15 of the asset shall be substituted for its adjusted  
16 basis.

17 “(2) EXCEPTION FOR DEPRECIATION, ETC.—  
18 The deduction for depreciation, depletion, and amor-  
19 tization shall be determined without regard to the  
20 application of paragraph (1) to the taxpayer or any  
21 other person.

22 “(b) INDEXED ASSET.—

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

25 “(A) stock in a corporation, and

1           “(B) 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)).

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

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

11          “(B) OPTIONS.—Any option or other right  
12          to acquire an interest in property.

13          “(C) NET LEASE PROPERTY.—In the case  
14          of a lessor, net lease property (within the mean-  
15          ing of subsection (i)(3)).

16          “(D) CERTAIN PREFERRED STOCK.—Stock  
17          which is fixed and preferred as to dividends and  
18          does not participate in corporate growth to any  
19          significant extent.

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

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

24          “(3) EXCEPTION FOR STOCK IN FOREIGN COR-  
25          PORATION WHICH IS REGULARLY TRADED ON NA-

1 TIONAL OR REGIONAL EXCHANGE.—Paragraph  
2 (2)(E) shall not apply to stock in a foreign corpora-  
3 tion the stock of which is listed on the New York  
4 Stock Exchange, the American Stock Exchange, the  
5 national market system operated by the National As-  
6 sociation of Securities Dealers, or any domestic re-  
7 gional exchange for which quotations are published  
8 on a regular basis other than—

9 “(A) stock of a foreign investment com-  
10 pany (within the meaning of section 1246(b)),

11 “(B) stock in a passive foreign investment  
12 company (as defined in section 1296), and

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

16 “(4) TREATMENT OF AMERICAN DEPOSITORY  
17 RECEIPTS.—For purposes of this section, an Amer-  
18 ican depository receipt for stock in a foreign cor-  
19 poration shall be treated as stock in such corpora-  
20 tion.

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

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

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

3           “(B) the applicable inflation ratio.

4           “(2) APPLICABLE INFLATION RATIO.—The ap-  
5           plicable inflation ratio for any asset 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 asset 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 asset 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) SHORT SALES.—

23           “(1) IN GENERAL.—In the case of a short sale  
24           of an indexed asset with a short sale period in excess  
25           of 1 year, for purposes of this title, the amount real-

1        ized shall be an amount equal to the amount realized  
2        (determined without regard to this paragraph) mul-  
3        tiplied by the applicable inflation ratio. In applying  
4        subsection (c)(2) for purposes of the preceding sen-  
5        tence, the date on which the property is sold short  
6        shall be treated as the date of acquisition and the  
7        closing date for the sale shall be treated as the date  
8        of disposition.

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

16            “(3) SHORT SALE PERIOD.—For purposes of  
17        this subsection, the short sale period begins on the  
18        day after property is sold and ends on the closing  
19        date for the sale.

20            “(e) TREATMENT OF REGULATED INVESTMENT  
21        COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

22            “(1) ADJUSTMENTS AT ENTITY LEVEL.—

23            “(A) IN GENERAL.—Except as otherwise  
24        provided in this paragraph, the adjustment  
25        under subsection (a) shall be allowed to any

1 qualified investment entity (including for pur-  
2 poses of determining the earnings and profits of  
3 such entity).

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

7 “(2) ADJUSTMENTS TO INTERESTS HELD IN  
8 ENTITY.—

9 “(A) IN GENERAL.—Stock in a qualified  
10 investment entity shall be an indexed asset for  
11 any calendar month in the same ratio as the  
12 fair market value of the assets held by such en-  
13 tity at the close of such month which are in-  
14 dexed assets bears to the fair market value of  
15 all assets of such entity at the close of such  
16 month.

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

22 “(C) RATIO OF 10 PERCENT OR LESS.—If  
23 the ratio for any calendar month determined  
24 under subparagraph (A) would (but for this

1           subparagraph) be 10 percent or less, such ratio  
2           for such month shall be zero.

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

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

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

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

20          “(f) OTHER PASS-THRU ENTITIES.—

21                  “(1) PARTNERSHIPS.—In the case of a partner-  
22                  ship, the adjustment made under subsection (a) at  
23                  the partnership level shall be passed through to the  
24                  partners.

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.

5           “(3) COMMON TRUST FUNDS.—In the case of a  
6 common trust fund, the adjustment made under sub-  
7 section (a) at the trust level shall be passed through  
8 to the participants.

9           “(g) DISPOSITIONS BETWEEN RELATED PERSONS.—

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

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

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

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

22           “(h) TRANSFERS TO INCREASE INDEXING ADJUST-  
23 MENT.—If any person transfers cash, debt, or any other  
24 property to another person and the principal purpose of  
25 such transfer is to secure or increase an adjustment under

1 subsection (a), the Secretary may disallow part or all of  
2 such adjustment or increase.

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

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

7 “(A) A substantial improvement to prop-  
8 erty.

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

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

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

19 “(3) NET LEASE PROPERTY DEFINED.—The  
20 term ‘net lease property’ means leased property  
21 where—

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

1           “(B) for the period of the lease, the sum  
2           of the deductions with respect to such property  
3           which are allowable to the lessor solely by rea-  
4           son of section 162 (other than rents and reim-  
5           bursed amounts with respect to such property)  
6           is 15 percent or less of the rental income pro-  
7           duced by such property.

8           “(4) TREATMENT OF CERTAIN DISTRIBUTIONS.—A distribution with respect to stock in a  
9           corporation which is not a dividend shall be treated  
10          as a disposition.

12          “(5) SECTION CANNOT INCREASE ORDINARY  
13          LOSS.—To the extent that (but for this paragraph)  
14          this section would create or increase a net ordinary  
15          loss to which section 1231(a)(2) applies or an ordi-  
16          nary loss to which any other provision of this title  
17          applies, such provision shall not apply. The taxpayer  
18          shall be treated as having a long-term capital loss in  
19          an amount equal to the amount of the ordinary loss  
20          to which the preceding sentence applies.

21          “(6) ACQUISITION DATE WHERE THERE HAS  
22          BEEN PRIOR APPLICATION OF SUBSECTION (a)(1)  
23          WITH RESPECT TO THE TAXPAYER.—If there has  
24          been a prior application of subsection (a)(1) to an  
25          asset while such asset was held by the taxpayer, the

1 date of acquisition of such asset by the taxpayer  
2 shall be treated as not earlier than the date of the  
3 most recent such prior application.

4 “(7) COLLAPSIBLE CORPORATIONS.—The appli-  
5 cation of section 341(a) (relating to collapsible cor-  
6 porations) shall be determined without regard to this  
7 section.

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

11 (b) CLERICAL AMENDMENT.—The table of sections  
12 for part II of subchapter O of chapter 1 of such Code  
13 is amended by inserting after the item relating to section  
14 1021 the following new item:

“Sec. 1022. Indexing of certain assets for purposes of determining  
gain or loss.”

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

1           “(3) EFFECT ON EARNINGS AND PROFITS OF  
2 INDEXED BASIS.—

**For substitution of indexed basis for adjusted basis in the case of the disposition of certain assets, see section 1022(a)(1).”**

3           (d) EFFECTIVE DATE.—The amendments made by  
4 this section shall apply to dispositions after December 31,  
5 1994, in taxable years ending after such date.

6 **SEC. 4. CAPITAL LOSS DEDUCTION ALLOWED WITH RE-**  
7 **SPECT TO SALE OR EXCHANGE OF PRINCIPAL**  
8 **RESIDENCE.**

9           (a) IN GENERAL.—Subsection (c) of section 165 of  
10 the Internal Revenue Code of 1986 (relating to limitation  
11 on losses of individuals) is amended by striking “and” at  
12 the end of paragraph (2), by striking the period at the  
13 end of paragraph (3) and inserting “; and”, and by adding  
14 at the end the following new paragraph:

15           “(4) losses arising from the sale or exchange of  
16 the principal residence (within the meaning of sec-  
17 tion 1034) of the taxpayer.”

18           (b) EFFECTIVE DATE.—The amendment made by  
19 subsection (a) shall apply to sales and exchanges after De-  
20 cember 31, 1994, in taxable years ending after such date.

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