

ADOPTION PROMOTION AND STABILITY ACT OF 1996

MAY 3, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered be printed

Mr. ARCHER, from the Committee on Ways and Means,
 submitted the following

R E P O R T

[To accompany H.R. 3286]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 3286) to help families defray adoption costs, and to promote the adoption of minority children, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

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The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. SHORT TITLE.

This Act may be cited as the “Adoption Promotion and Stability Act of 1996”.

SEC. 2. TABLE OF CONTENTS.

The table of contents of this Act is as follows:

Sec. 1. Short title.
Sec. 2. Table of contents.

TITLE I—CREDIT FOR ADOPTION EXPENSES

Sec. 101. Credit for adoption expenses.

TITLE II—INTERETHNIC ADOPTION

Sec. 201. Removal of barriers to interethnic adoption.

TITLE III—CHILD CUSTODY PROCEEDINGS AFFECTED BY THE INDIAN CHILD WELFARE ACT OF 1978

Sec. 301. Inapplicability of the Indian Child Welfare Act of 1978 to child custody proceedings involving a child whose parents do not maintain affiliation with their Indian tribe.
Sec. 302. Membership and child custody proceedings.
Sec. 303. Effective date.

TITLE IV—REVENUE OFFSETS

Sec. 400. Amendment of 1986 Code.

Subtitle A—Exclusion for Energy Conservation Subsidies Limited to Subsidies With Respect to Dwelling Units

Sec. 401. Exclusion for energy conservation subsidies limited to subsidies with respect to dwelling units.

Subtitle B—Foreign Trust Tax Compliance

Sec. 411. Improved information reporting on foreign trusts.
Sec. 412. Comparable penalties for failure to file return relating to transfers to foreign entities.
Sec. 413. Modifications of rules relating to foreign trusts having one or more United States beneficiaries.
Sec. 414. Foreign persons not to be treated as owners under grantor trust rules.
Sec. 415. Information reporting regarding foreign gifts.
Sec. 416. Modification of rules relating to foreign trusts which are not grantor trusts.
Sec. 417. Residence of trusts, etc.

TITLE I—CREDIT FOR ADOPTION EXPENSES

SEC. 101. CREDIT FOR ADOPTION EXPENSES.

(a) **IN GENERAL.**—Subpart A of part IV of subchapter A of chapter 1 of the Internal Revenue Code of 1986 (relating to nonrefundable personal credits) is amended by inserting after section 22 the following new section:

“SEC. 23. ADOPTION EXPENSES.

“(a) **ALLOWANCE OF CREDIT.**—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year the amount of the qualified adoption expenses paid or incurred by the taxpayer during such taxable year.

“(b) **LIMITATIONS.**—

“(1) **DOLLAR LIMITATION.**—The aggregate amount of qualified adoption expenses which may be taken into account under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed \$5,000.

“(2) **INCOME LIMITATION.**—The amount allowable as a credit under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so allowable (determined without regard to this paragraph but with regard to paragraph (1)) as—

“(A) the amount (if any) by which the taxpayer’s adjusted gross income (determined without regard to sections 911, 931, and 933) exceeds \$75,000, bears to

“(B) \$40,000.

“(3) **DENIAL OF DOUBLE BENEFIT.**—

“(A) **IN GENERAL.**—No credit shall be allowed under subsection (a) for any expense for which a deduction or credit is allowable under any other provision of this chapter.

“(B) GRANTS.—No credit shall be allowed under subsection (a) for any expense to the extent that funds for such expense are received under any Federal, State, or local program. The preceding sentence shall not apply to expenses for the adoption of a child with special needs.

“(C) REIMBURSEMENT.—No credit shall be allowed under subsection (a) for any expense to the extent that such expense is reimbursed and the reimbursement is excluded from gross income under section 137.

“(c) CARRYFORWARDS OF UNUSED CREDIT.—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of the credits allowable under this subpart (other than this section), such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such taxable year. No credit may be carried forward under this subsection to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For purposes of the preceding sentence, credits shall be treated as used on a first-in first-out basis.

“(d) DEFINITIONS.—For purposes of this section—

“(1) QUALIFIED ADOPTION EXPENSES.—The term ‘qualified adoption expenses’ means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses—

“(A) which are directly related to, and the principal purpose of which is for, the legal adoption of an eligible child by the taxpayer, and

“(B) which are not incurred in violation of State or Federal law or in carrying out any surrogate parenting arrangement.

“(2) EXPENSES FOR ADOPTION OF SPOUSE’S CHILD NOT ELIGIBLE.—The term ‘qualified adoption expenses’ shall not include any expenses in connection with the adoption by an individual of a child who is the child of such individual’s spouse.

“(3) ELIGIBLE CHILD.—The term ‘eligible child’ means any individual—

“(A) who has not attained age 18 as of the time of the adoption, or

“(B) who is physically or mentally incapable of caring for himself.

“(4) CHILD WITH SPECIAL NEEDS.—The term ‘child with special needs’ means any child if—

“(A) a State has determined that the child cannot or should not be returned to the home of his parents, and

“(B) such State has determined that there exists with respect to the child a specific factor or condition (such as his ethnic background, age, or membership in a minority or sibling group, or the presence of factors such as medical conditions or physical, mental, or emotional handicaps) because of which it is reasonable to conclude that such child cannot be placed with adoptive parents without providing adoption assistance.

“(e) SPECIAL RULES FOR FOREIGN ADOPTIONS.—In the case of a foreign adoption—

“(1) subsection (a) shall not apply to any qualified adoption expense with respect to such adoption unless such adoption becomes final, and

“(2) any such expense which is paid or incurred before the taxable year in which such adoption becomes final shall be taken into account under this section as if such expense were paid or incurred during such year.

“(f) MARRIED COUPLES MUST FILE JOINT RETURNS.—Rules similar to the rules of paragraphs (2), (3), and (4) of section 21(e) shall apply for purposes of this section.

“(g) BASIS ADJUSTMENTS.—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

“(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out this section and section 137, including regulations which treat unmarried individuals who pay or incur qualified adoption expenses with respect to the same child as 1 taxpayer for purposes of applying the dollar limitation in subsection (b)(1) of this section and in section 137(b)(1).”

(b) EXCLUSION OF AMOUNTS RECEIVED UNDER EMPLOYER’S ADOPTION ASSISTANCE PROGRAMS.—Part III of subchapter B of chapter 1 of such Code (relating to items specifically excluded from gross income) is amended by redesignating section 137 as section 138 and by inserting after section 136 the following new section:

“SEC. 137. ADOPTION ASSISTANCE PROGRAMS.

“(a) IN GENERAL.—Gross income of an employee does not include amounts paid or expenses incurred by the employer for qualified adoption expenses in connection with the adoption of a child by an employee if such amounts are furnished pursuant to an adoption assistance program.

“(b) LIMITATIONS.—

“(1) DOLLAR LIMITATION.—The aggregate amount excludable from gross income under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed \$5,000.

“(2) INCOME LIMITATION.—The amount excludable from gross income under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so excludable (determined without regard to this paragraph but with regard to paragraph (1)) as—

“(A) the amount (if any) by which the taxpayer’s adjusted gross income exceeds \$75,000, bears to

“(B) \$40,000.

“(3) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of paragraph (2), adjusted gross income shall be determined—

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

“(B) after the application of sections 86, 135, 219, and 469.

“(c) ADOPTION ASSISTANCE PROGRAM.—For purposes of this section, an adoption assistance program is a plan of an employer—

“(1) under which the employer provides employees with adoption assistance, and

“(2) which meets requirements similar to the requirements of paragraphs (2), (3), and (5) of section 127(b).

An adoption reimbursement program operated under section 1052 of title 10, United States Code (relating to armed forces) or section 514 of title 14, United States Code (relating to members of the Coast Guard) shall be treated as an adoption assistance program for purposes of this section.

“(d) QUALIFIED ADOPTION EXPENSES.—For purposes of this section, the term ‘qualified adoption expenses’ has the meaning given such term by section 23(d).

“(e) CERTAIN RULES TO APPLY.—Rules similar to the rules of subsections (e) and (g) of section 23 shall apply for purposes of this section.”.

(c) CONFORMING AMENDMENTS.—

(1) Sections 86(b)(2)(A) and 135(c)(4)(A) of such Code are each amended by inserting “137,” before “911”.

(2) Clause (i) of section 219(g)(3)(A) of such Code is amended by inserting “, 137,” before “and 911”.

(3) Clause (ii) of section 469(i)(3)(E) of such Code is amended to read as follows:

“(ii) the amounts excludable from gross income under sections 135 and 137,”.

(4) Subsection (a) of section 1016 of such Code is amended by striking “and” at the end of paragraph (24), by striking the period at the end of paragraph (25) and inserting “, and”, and by adding at the end the following new paragraph:

“(26) to the extent provided in sections 23(g) and 137(e).”

(5) The table of sections for subpart A of part IV of subchapter A of chapter 1 of such Code is amended by inserting after the item relating to section 22 the following new item:

“Sec. 23. Adoption expenses.”.

(6) The table of sections for part III of subchapter B of chapter 1 of such Code is amended by striking the item relating to section 137 and inserting the following:

“Sec. 137. Adoption assistance programs.
“Sec. 138. Cross reference to other Acts.”.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

TITLE II—INTERETHNIC ADOPTION

SEC. 201. REMOVAL OF BARRIERS TO INTERETHNIC ADOPTION.

(a) STATE PLAN REQUIREMENTS.—Section 471(a) of the Social Security Act (42 U.S.C 671(a)) is amended—

(1) by striking “and” at the end of paragraph (16);

(2) by striking the period at the end of paragraph (17) and inserting “, and”; and

(3) by adding at the end the following:

“(18) not later than January 1, 1997, provides that neither the State nor any other entity in the State that receives funds from the Federal Government and is involved in adoption or foster care placements may—

“(A) deny to any person the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the person, or of the child, involved; or

“(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.”

(b) ENFORCEMENT.—Section 474 of such Act (42 U.S.C. 674) is amended by adding at the end the following:

“(d)(1) If a State’s program operated under this part is found, as a result of a review conducted under section 1123, to have violated section 471(a)(18) during a quarter with respect to any person, then, notwithstanding subsection (a) of this section and any regulations promulgated under section 1123(b)(3), the Secretary shall reduce the amount otherwise payable to the State under this part, for the quarter and for each subsequent quarter before the 1st quarter for which the State program is found, as a result of such a review, not to have violated section 471(a)(18) with respect to any person, by—

“(A) 2 percent of such otherwise payable amount, in the case of the 1st such finding with respect to the State;

“(B) 5 percent of such otherwise payable amount, in the case of the 2nd such finding with respect to the State; or

“(C) 10 percent of such otherwise payable amount, in the case of the 3rd or subsequent such finding with respect to the State.

“(2) Any other entity which is in a State that receives funds under this part and which violates section 471(a)(18) during a quarter with respect to any person shall remit to the Secretary all funds that were paid by the State to the entity during the quarter from such funds.

“(3)(A) Any individual who is aggrieved by a violation of section 471(a)(18) by a State or other entity may bring an action seeking relief from the State or other entity in any United States district court.

“(B) An action under this paragraph may not be brought more than 2 years after the date the alleged violation occurred.

“(4) This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.”

(c) CIVIL RIGHTS.—

(1) PROHIBITED CONDUCT.—A person or government that is involved in adoption or foster care placements may not—

(A) deny to any individual the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the individual, or of the child, involved; or

(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.

(2) ENFORCEMENT.—Noncompliance with paragraph (1) is deemed a violation of title VI of the Civil Rights Act of 1964.

(3) NO EFFECT ON THE INDIAN CHILD WELFARE ACT OF 1978.—This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.

(d) CONFORMING REPEAL.—Section 553 of the Howard M. Metzenbaum Multiethnic Placement Act of 1994 (42 U.S.C. 5115a) is repealed.

TITLE III—CHILD CUSTODY PROCEEDINGS AFFECTED BY THE INDIAN CHILD WELFARE ACT OF 1978

SEC. 301. INAPPLICABILITY OF THE INDIAN CHILD WELFARE ACT OF 1978 TO CHILD CUSTODY PROCEEDINGS INVOLVING A CHILD WHOSE PARENTS DO NOT MAINTAIN AFFILIATION WITH THEIR INDIAN TRIBE.

Title I of the Indian Child Welfare Act of 1978 (25 U.S.C. 1911 et seq.) is amended by adding at the end the following:

“SEC. 114. (a) This title does not apply to any child custody proceeding involving a child who does not reside or is not domiciled within a reservation unless—

“(1) at least one of the child’s biological parents is of Indian descent; and

“(2) at least one of the child’s biological parents maintains significant social, cultural, or political affiliation with the Indian tribe of which either parent is a member.

“(b) The factual determination as to whether a biological parent maintains significant social, cultural, or political affiliation with the Indian tribe of which either parent is a member shall be based on such affiliation as of the time of the child custody proceeding.

“(c) The determination that this title does not apply pursuant to subsection (a) is final, and, thereafter, this title shall not be the basis for determining jurisdiction over any child custody proceeding involving the child.”.

SEC. 302. MEMBERSHIP AND CHILD CUSTODY PROCEEDINGS.

Title I of the Indian Child Welfare Act of 1978 (25 U.S.C. 1911 et seq.), as amended by section 301 of this title, is further amended by adding at the end the following:

“SEC. 115. (a) A person who attains the age of 18 years before becoming a member of an Indian tribe may become a member of an Indian tribe only upon the person’s written consent.

“(b) For the purposes of any child custody proceeding involving an Indian child, membership in an Indian tribe shall be effective from the actual date of admission to membership in the Indian tribe and shall not be given retroactive effect.”.

SEC. 303. EFFECTIVE DATE.

The amendments made by this title shall take effect on the date of the enactment of this Act and shall apply with respect to any child custody proceeding in which a final decree has not been entered as of such date.

TITLE IV—REVENUE OFFSETS

SEC. 400. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

Subtitle A—Exclusion for Energy Conservation Subsidies Limited to Subsidies With Respect to Dwelling Units

SEC. 401. EXCLUSION FOR ENERGY CONSERVATION SUBSIDIES LIMITED TO SUBSIDIES WITH RESPECT TO DWELLING UNITS.

(a) IN GENERAL.—Paragraph (1) of section 136(c) (defining energy conservation measure) is amended by striking “energy demand—” and all that follows and inserting “energy demand with respect to a dwelling unit.”

(b) CONFORMING AMENDMENTS.—

(1) Subsection (a) of section 136 is amended to read as follows:

“(a) EXCLUSION.—Gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure.”

(2) Paragraph (2) of section 136(c) is amended—

(A) by striking subparagraph (A) and by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively, and

(B) by striking “AND SPECIAL RULES” in the paragraph heading.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after December 31, 1996, unless received pursuant to a written binding contract in effect on September 13, 1995, and at all times thereafter.

Subtitle B—Foreign Trust Tax Compliance

SEC. 411. IMPROVED INFORMATION REPORTING ON FOREIGN TRUSTS.

(a) IN GENERAL.—Section 6048 (relating to returns as to certain foreign trusts) is amended to read as follows:

“SEC. 6048. INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.**“(a) NOTICE OF CERTAIN EVENTS.—**

“(1) GENERAL RULE.—On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).

“(2) CONTENTS OF NOTICE.—The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—

“(A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and

“(B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.

“(3) REPORTABLE EVENT.—For purposes of this subsection—

“(A) IN GENERAL.—The term ‘reportable event’ means—

“(i) the creation of any foreign trust by a United States person,

“(ii) the transfer of any money or property (directly or indirectly) to a foreign trust by a United States person, including a transfer by reason of death, and

“(iii) the death of a citizen or resident of the United States if—

“(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

“(II) any portion of a foreign trust was included in the gross estate of the decedent.

“(B) EXCEPTIONS.—

“(i) FAIR MARKET VALUE SALES.—Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

“(ii) DEFERRED COMPENSATION AND CHARITABLE TRUSTS.—Subparagraph (A) shall not apply with respect to a trust which is—

“(I) described in section 402(b), 404(a)(4), or 404A, or

“(II) determined by the Secretary to be described in section 501(c)(3).

“(4) RESPONSIBLE PARTY.—For purposes of this subsection, the term ‘responsible party’ means—

“(A) the grantor in the case of the creation of an inter vivos trust,

“(B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and

“(C) the executor of the decedent’s estate in any other case.

“(b) UNITED STATES GRANTOR OF FOREIGN TRUST.—

“(1) IN GENERAL.—If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall be responsible to ensure that—

“(A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and

“(B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.

“(2) TRUSTS NOT HAVING UNITED STATES AGENT.—

“(A) IN GENERAL.—If the rules of this paragraph apply to any foreign trust, the determination of amounts required to be taken into account with respect to such trust by a United States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

“(B) UNITED STATES AGENT REQUIRED.—The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust’s limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—

“(i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or

“(ii) any summons by the Secretary for such records or testimony.

The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints an agent described in this subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

“(C) OTHER RULES TO APPLY.—Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.

“(c) REPORTING BY UNITED STATES BENEFICIARIES OF FOREIGN TRUSTS.—

“(1) IN GENERAL.—If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—

“(A) the name of such trust,

“(B) the aggregate amount of the distributions so received from such trust during such taxable year, and

“(C) such other information as the Secretary may prescribe.

“(2) INCLUSION IN INCOME IF RECORDS NOT PROVIDED.—

“(A) IN GENERAL.—If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To the extent provided in regulations, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b)(2)(B).

“(B) APPLICATION OF ACCUMULATION DISTRIBUTION RULES.—For purposes of applying section 668 in a case to which subparagraph (A) applies, the applicable number of years for purposes of section 668(a) shall be $\frac{1}{2}$ of the number of years the trust has been in existence.

“(d) SPECIAL RULES.—

“(1) DETERMINATION OF WHETHER UNITED STATES PERSON MAKES TRANSFER OR RECEIVES DISTRIBUTION.—For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

“(2) DOMESTIC TRUSTS WITH FOREIGN ACTIVITIES.—To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

“(3) TIME AND MANNER OF FILING INFORMATION.—Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

“(4) MODIFICATION OF RETURN REQUIREMENTS.—The Secretary is authorized to suspend or modify any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.”.

(b) INCREASED PENALTIES.—Section 6677 (relating to failure to file information returns with respect to certain foreign trusts) is amended to read as follows:

“SEC. 6677. FAILURE TO FILE INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

“(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—

“(1) is not filed on or before the time provided in such section, or

“(2) does not include all the information required pursuant to such section or includes incorrect information,

the person required to file such notice or return shall pay a penalty equal to 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of \$10,000 for each 30-day period (or fraction thereof) during which such failure con-

tinues after the expiration of such 90-day period. In no event shall the penalty under this subsection with respect to any failure exceed the gross reportable amount.

“(b) SPECIAL RULES FOR RETURNS UNDER SECTION 6048(b).—In the case of a return required under section 6048(b)—

“(1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and

“(2) subsection (a) shall be applied by substituting ‘5 percent’ for ‘35 percent’.

“(c) GROSS REPORTABLE AMOUNT.—For purposes of subsection (a), the term ‘gross reportable amount’ means—

“(1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),

“(2) the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and

“(3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

“(d) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information is not reasonable cause.

“(e) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).”

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 6724(d) is amended by striking “or” at the end of subparagraph (S), by striking the period at the end of subparagraph (T) and inserting “, or”, and by inserting after subparagraph (T) the following new subparagraph:

“(U) section 6048(b)(1)(B) (relating to foreign trust reporting requirements).”

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the item relating to section 6048 and inserting the following new item:

“Sec. 6048. Information with respect to certain foreign trusts.”

(3) The table of sections for part I of subchapter B of chapter 68 is amended by striking the item relating to section 6677 and inserting the following new item:

“Sec. 6677. Failure to file information with respect to certain foreign trusts.”

(d) EFFECTIVE DATES.—

(1) REPORTABLE EVENTS.—To the extent related to subsection (a) of section 6048 of the Internal Revenue Code of 1986, as amended by this section, the amendments made by this section shall apply to reportable events (as defined in such section 6048) occurring after the date of the enactment of this Act.

(2) GRANTOR TRUST REPORTING.—To the extent related to subsection (b) of such section 6048, the amendments made by this section shall apply to taxable years of United States persons beginning after December 31, 1995.

(3) REPORTING BY UNITED STATES BENEFICIARIES.—To the extent related to subsection (c) of such section 6048, the amendments made by this section shall apply to distributions received after the date of the enactment of this Act.

SEC. 412. COMPARABLE PENALTIES FOR FAILURE TO FILE RETURN RELATING TO TRANSFERS TO FOREIGN ENTITIES.

(a) IN GENERAL.—Section 1494 is amended by adding at the end the following new subsection:

“(c) PENALTY.—In the case of any failure to file a return required by the Secretary with respect to any transfer described in section 1491, the person required to file such return shall be liable for the penalties provided in section 6677 in the same manner as if such failure were a failure to file a notice under section 6048(a).”

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to transfers after the date of the enactment of this Act.

SEC. 413. MODIFICATIONS OF RULES RELATING TO FOREIGN TRUSTS HAVING ONE OR MORE UNITED STATES BENEFICIARIES.

(a) TREATMENT OF TRUST OBLIGATIONS, ETC.—

(1) Paragraph (2) of section 679(a) is amended by striking subparagraph (B) and inserting the following:

“(B) TRANSFERS AT FAIR MARKET VALUE.—To any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value.”.

(2) Subsection (a) of section 679 (relating to foreign trusts having one or more United States beneficiaries) is amended by adding at the end the following new paragraph:

“(3) CERTAIN OBLIGATIONS NOT TAKEN INTO ACCOUNT UNDER FAIR MARKET VALUE EXCEPTION.—

“(A) IN GENERAL.—In determining whether paragraph (2)(B) applies to any transfer by a person described in clause (ii) or (iii) of subparagraph (C), there shall not be taken into account—

“(i) except as provided in regulations, any obligation of a person described in subparagraph (C), and

“(ii) to the extent provided in regulations, any obligation which is guaranteed by a person described in subparagraph (C).

“(B) TREATMENT OF PRINCIPAL PAYMENTS ON OBLIGATION.—Principal payments by the trust on any obligation referred to in subparagraph (A) shall be taken into account on and after the date of the payment in determining the portion of the trust attributable to the property transferred.

“(C) PERSONS DESCRIBED.—The persons described in this subparagraph are—

“(i) the trust,

“(ii) any grantor or beneficiary of the trust, and

“(iii) any person who is related (within the meaning of section 643(i)(2)(B)) to any grantor or beneficiary of the trust.”.

(b) EXEMPTION OF TRANSFERS TO CHARITABLE TRUSTS.—Subsection (a) of section 679 is amended by striking “section 404(a)(4) or 404A” and inserting “section 6048(a)(3)(B)(ii)”.

(c) OTHER MODIFICATIONS.—Subsection (a) of section 679 is amended by adding at the end the following new paragraphs:

“(4) SPECIAL RULES APPLICABLE TO FOREIGN GRANTOR WHO LATER BECOMES A UNITED STATES PERSON.—

“(A) IN GENERAL.—If a nonresident alien individual has a residency starting date within 5 years after directly or indirectly transferring property to a foreign trust, this section and section 6048 shall be applied as if such individual transferred to such trust on the residency starting date an amount equal to the portion of such trust attributable to the property transferred by such individual to such trust in such transfer.

“(B) TREATMENT OF UNDISTRIBUTED INCOME.—For purposes of this section, undistributed net income for periods before such individual’s residency starting date shall be taken into account in determining the portion of the trust which is attributable to property transferred by such individual to such trust but shall not otherwise be taken into account.

“(C) RESIDENCY STARTING DATE.—For purposes of this paragraph, an individual’s residency starting date is the residency starting date determined under section 7701(b)(2)(A).

“(5) OUTBOUND TRUST MIGRATIONS.—If—

“(A) an individual who is a citizen or resident of the United States transferred property to a trust which was not a foreign trust, and

“(B) such trust becomes a foreign trust while such individual is alive, then this section and section 6048 shall be applied as if such individual transferred to such trust on the date such trust becomes a foreign trust an amount equal to the portion of such trust attributable to the property previously transferred by such individual to such trust. A rule similar to the rule of paragraph (4)(B) shall apply for purposes of this paragraph.”.

(d) MODIFICATIONS RELATING TO WHETHER TRUST HAS UNITED STATES BENEFICIARIES.—Subsection (c) of section 679 is amended by adding at the end the following new paragraph:

“(3) CERTAIN UNITED STATES BENEFICIARIES DISREGARDED.—A beneficiary shall not be treated as a United States person in applying this section with respect to any transfer of property to foreign trust if such beneficiary first became a United States person more than 5 years after the date of such transfer.”.

(e) TECHNICAL AMENDMENT.—Subparagraph (A) of section 679(c)(2) is amended to read as follows:

“(A) in the case of a foreign corporation, such corporation is a controlled foreign corporation (as defined in section 957(a)),”.

(f) REGULATIONS.—Section 679 is amended by adding at the end the following new subsection:

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

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to transfers of property after February 6, 1995.

SEC. 414. FOREIGN PERSONS NOT TO BE TREATED AS OWNERS UNDER GRANTOR TRUST RULES.

(a) GENERAL RULE.—

(1) Subsection (f) of section 672 (relating to special rule where grantor is foreign person) is amended to read as follows:

“(f) SUBPART NOT TO RESULT IN FOREIGN OWNERSHIP.—

“(1) IN GENERAL.—Notwithstanding any other provision of this subpart, this subpart shall apply only to the extent such application results in an amount (if any) being currently taken into account (directly or through 1 or more entities) under this chapter in computing the income of a citizen or resident of the United States or a domestic corporation.

“(2) EXCEPTIONS.—

“(A) CERTAIN REVOCABLE AND IRREVOCABLE TRUSTS.—Paragraph (1) shall not apply to any portion of a trust if—

“(i) the power to revest absolutely in the grantor title to the trust property to which such portion is attributable is exercisable solely by the grantor without the approval or consent of any other person or with the consent of a related or subordinate party who is subservient to the grantor, or

“(ii) the only amounts distributable from such portion (whether income or corpus) during the lifetime of the grantor are amounts distributable to the grantor or the spouse of the grantor.

“(B) COMPENSATORY TRUSTS.—Except as provided in regulations, paragraph (1) shall not apply to any portion of a trust distributions from which are taxable as compensation for services rendered.

“(3) SPECIAL RULES.—Except as otherwise provided in regulations prescribed by the Secretary—

“(A) a controlled foreign corporation (as defined in section 957) shall be treated as a domestic corporation for purposes of paragraph (1), and

“(B) paragraph (1) shall not apply for purposes of applying section 1296.

“(4) RECHARACTERIZATION OF PURPORTED GIFTS.—In the case of any transfer directly or indirectly from a partnership or foreign corporation which the transferee treats as a gift or bequest, the Secretary may recharacterize such transfer in such circumstances as the Secretary determines to be appropriate to prevent the avoidance of the purposes of this subsection.

“(5) SPECIAL RULE WHERE GRANTOR IS FOREIGN PERSON.—If—

“(A) but for this subsection, a foreign person would be treated as the owner of any portion of a trust, and

“(B) such trust has a beneficiary who is a United States person, such beneficiary shall be treated as the grantor of such portion to the extent such beneficiary or any member of such beneficiary’s family (within the meaning of section 267(c)(4)) has made (directly or indirectly) transfers of property (other than in a sale for full and adequate consideration) to such foreign person. For purposes of the preceding sentence, any gift shall not be taken into account to the extent such gift would be excluded from taxable gifts under section 2503(b).

“(6) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including regulations providing that paragraph (1) shall not apply in appropriate cases.”.

(2) The last sentence of subsection (c) of section 672 of such Code is amended by inserting “subsection (f) and” before “sections 674”.

(b) CREDIT FOR CERTAIN TAXES.—

(1) Paragraph (2) of section 665(d) is amended by adding at the end the following new sentence: “Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the term ‘taxes imposed on the trust’ includes the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign coun-

try or possession of the United States on the settlor or such other person in respect of trust income.”

(2) Paragraph (5) of section 901(b) is amended by adding at the end the following new sentence: “Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.”

(c) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—

(1) Section 643 is amended by adding at the end the following new subsection:

“(h) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—For purposes of this part, any amount paid to a United States person which is derived directly or indirectly from a foreign trust of which the payor is not the grantor shall be deemed in the year of payment to have been directly paid by the foreign trust to such United States person.”

(2) Section 665 is amended by striking subsection (c).

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided by paragraph (2), the amendments made by this section shall take effect on the date of the enactment of this Act.

(2) EXCEPTION FOR CERTAIN TRUSTS.—The amendments made by this section shall not apply to any trust—

(A) which is treated as owned by the grantor under section 676 or 677 (other than subsection (a)(3) thereof) of the Internal Revenue Code of 1986, and

(B) which is in existence on September 19, 1995.

The preceding sentence shall not apply to the portion of any such trust attributable to any transfer to such trust after September 19, 1995.

(e) TRANSITIONAL RULE.—If—

(1) by reason of the amendments made by this section, any person other than a United States person ceases to be treated as the owner of a portion of a domestic trust, and

(2) before January 1, 1997, such trust becomes a foreign trust, or the assets of such trust are transferred to a foreign trust, no tax shall be imposed by section 1491 of the Internal Revenue Code of 1986 by reason of such trust becoming a foreign trust or the assets of such trust being transferred to a foreign trust.

SEC. 415. INFORMATION REPORTING REGARDING FOREIGN GIFTS.

(a) IN GENERAL.—Subpart A of part III of subchapter A of chapter 61 is amended by inserting after section 6039E the following new section:

“SEC. 6039F. NOTICE OF LARGE GIFTS RECEIVED FROM FOREIGN PERSONS.

“(a) IN GENERAL.—If the value of the aggregate foreign gifts received by a United States person (other than an organization described in section 501(c) and exempt from tax under section 501(a)) during any taxable year exceeds \$10,000, such United States person shall furnish (at such time and in such manner as the Secretary shall prescribe) such information as the Secretary may prescribe regarding each foreign gift received during such year.

“(b) FOREIGN GIFT.—For purposes of this section, the term ‘foreign gift’ means any amount received from a person other than a United States person which the recipient treats as a gift or bequest. Such term shall not include any qualified transfer (within the meaning of section 2503(e)(2)) or any distribution properly disclosed in a return under section 6048(c).

“(c) PENALTY FOR FAILURE TO FILE INFORMATION.—

“(1) IN GENERAL.—If a United States person fails to furnish the information required by subsection (a) with respect to any foreign gift within the time prescribed therefor (including extensions)—

“(A) the tax consequences of the receipt of such gift shall be determined by the Secretary, and

“(B) such United States person shall pay (upon notice and demand by the Secretary and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month for which the failure continues (not to exceed 25 percent of such amount in the aggregate).

“(2) REASONABLE CAUSE EXCEPTION.—Paragraph (1) shall not apply to any failure to report a foreign gift if the United States person shows that the failure is due to reasonable cause and not due to willful neglect.

“(d) COST-OF-LIVING ADJUSTMENT.—In the case of any taxable year beginning after December 31, 1996, the \$10,000 amount under subsection (a) shall be in-

creased by an amount equal to the product of such amount and the cost-of-living adjustment for such taxable year under section 1(f)(3), except that subparagraph (B) thereof shall be applied by substituting '1995' for '1992'.

"(e) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section."

(b) CLERICAL AMENDMENT.—The table of sections for such subpart is amended by inserting after the item relating to section 6039E the following new item:

"Sec. 6039F. Notice of large gifts received from foreign persons."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after the date of the enactment of this Act in taxable years ending after such date.

SEC. 416. MODIFICATION OF RULES RELATING TO FOREIGN TRUSTS WHICH ARE NOT GRANT-OR TRUSTS.

(a) MODIFICATION OF INTEREST CHARGE ON ACCUMULATION DISTRIBUTIONS.—Subsection (a) of section 668 (relating to interest charge on accumulation distributions from foreign trusts) is amended to read as follows:

"(a) GENERAL RULE.—For purposes of the tax determined under section 667(a)—

"(1) INTEREST DETERMINED USING UNDERPAYMENT RATES.—The interest charge determined under this section with respect to any distribution is the amount of interest which would be determined on the partial tax computed under section 667(b) for the period described in paragraph (2) using the rates and the method under section 6621 applicable to underpayments of tax.

"(2) PERIOD.—For purposes of paragraph (1), the period described in this paragraph is the period which begins on the date which is the applicable number of years before the date of the distribution and which ends on the date of the distribution.

"(3) APPLICABLE NUMBER OF YEARS.—For purposes of paragraph (2)—

"(A) IN GENERAL.—The applicable number of years with respect to a distribution is the number determined by dividing—

"(i) the sum of the products described in subparagraph (B) with respect to each undistributed income year, by

"(ii) the aggregate undistributed net income.

The quotient determined under the preceding sentence shall be rounded under procedures prescribed by the Secretary.

"(B) PRODUCT DESCRIBED.—For purposes of subparagraph (A), the product described in this subparagraph with respect to any undistributed income year is the product of—

"(i) the undistributed net income for such year, and

"(ii) the sum of the number of taxable years between such year and the taxable year of the distribution (counting in each case the undistributed income year but not counting the taxable year of the distribution).

"(4) UNDISTRIBUTED INCOME YEAR.—For purposes of this subsection, the term 'undistributed income year' means any prior taxable year of the trust for which there is undistributed net income, other than a taxable year during all of which the beneficiary receiving the distribution was not a citizen or resident of the United States.

"(5) DETERMINATION OF UNDISTRIBUTED NET INCOME.—Notwithstanding section 666, for purposes of this subsection, an accumulation distribution from the trust shall be treated as reducing proportionately the undistributed net income for undistributed income years.

"(6) PERIODS BEFORE 1996.—Interest for the portion of the period described in paragraph (2) which occurs before January 1, 1996, shall be determined—

"(A) by using an interest rate of 6 percent, and

"(B) without compounding until January 1, 1996."

(b) ABUSIVE TRANSACTIONS.—Section 643(a) is amended by inserting after paragraph (6) the following new paragraph:

"(7) ABUSIVE TRANSACTIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent avoidance of such purposes."

(c) TREATMENT OF LOANS FROM TRUSTS.—

(1) IN GENERAL.—Section 643 (relating to definitions applicable to subparts A, B, C, and D) is amended by adding at the end the following new subsection:

"(i) LOANS FROM FOREIGN TRUSTS.—For purposes of subparts B, C, and D—

"(1) GENERAL RULE.—Except as provided in regulations, if a foreign trust makes a loan of cash or marketable securities directly or indirectly to—

“(A) any grantor or beneficiary of such trust who is a United States person, or

“(B) any United States person not described in subparagraph (A) who is related to such grantor or beneficiary,
the amount of such loan shall be treated as a distribution by such trust to such grantor or beneficiary (as the case may be).

“(2) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

“(A) CASH.—The term ‘cash’ includes foreign currencies and cash equivalents.

“(B) RELATED PERSON.—

“(i) IN GENERAL.—A person is related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the preceding sentence, section 267(c)(4) shall be applied as if the family of an individual includes the spouses of the members of the family.

“(ii) ALLOCATION.—If any person described in paragraph (1)(B) is related to more than one person, the grantor or beneficiary to whom the treatment under this subsection applies shall be determined under regulations prescribed by the Secretary.

“(C) EXCLUSION OF TAX-EXEMPTS.—The term ‘United States person’ does not include any entity exempt from tax under this chapter.

“(D) TRUST NOT TREATED AS SIMPLE TRUST.—Any trust which is treated under this subsection as making a distribution shall be treated as not described in section 651.

“(3) SUBSEQUENT TRANSACTIONS REGARDING LOAN PRINCIPAL.—If any loan is taken into account under paragraph (1), any subsequent transaction between the trust and the original borrower regarding the principal of the loan (by way of complete or partial repayment, satisfaction, cancellation, discharge, or otherwise) shall be disregarded for purposes of this title.”

(2) TECHNICAL AMENDMENT.—Paragraph (8) of section 7872(f) is amended by inserting “, 643(i),” before “or 1274” each place it appears.

(d) EFFECTIVE DATES.—

(1) INTEREST CHARGE.—The amendment made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

(2) ABUSIVE TRANSACTIONS.—The amendment made by subsection (b) shall take effect on the date of the enactment of this Act.

(3) LOANS FROM TRUSTS.—The amendment made by subsection (c) shall apply to loans of cash or marketable securities made after September 19, 1995.

SEC. 417. RESIDENCE OF TRUSTS, ETC.

(a) TREATMENT AS UNITED STATES PERSON.—

(1) IN GENERAL.—Paragraph (30) of section 7701(a) is amended by striking “and” at the end of subparagraph (C) and by striking subparagraph (D) and by inserting the following new subparagraphs:

“(D) any estate (other than a foreign estate, within the meaning of paragraph (31)), and

“(E) any trust if—

“(i) a court within the United States is able to exercise primary supervision over the administration of the trust, and

“(ii) one or more United States fiduciaries have the authority to control all substantial decisions of the trust.”

(2) CONFORMING AMENDMENT.—Paragraph (31) of section 7701(a) is amended to read as follows:

“(31) FOREIGN ESTATE OR TRUST.—

“(A) FOREIGN ESTATE.—The term ‘foreign estate’ means an estate the income of which, from sources without the United States which is not effectively connected with the conduct of a trade or business within the United States, is not includible in gross income under subtitle A.

“(B) FOREIGN TRUST.—The term ‘foreign trust’ means any trust other than a trust described in subparagraph (E) of paragraph (30).”

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply—

(A) to taxable years beginning after December 31, 1996, or

(B) at the election of the trustee of a trust, to taxable years ending after the date of the enactment of this Act.

Such an election, once made, shall be irrevocable.

(b) DOMESTIC TRUSTS WHICH BECOME FOREIGN TRUSTS.—

(1) IN GENERAL.—Section 1491 (relating to imposition of tax on transfers to avoid income tax) is amended by adding at the end the following new flush sentence:

“If a trust which is not a foreign trust becomes a foreign trust, such trust shall be treated for purposes of this section as having transferred, immediately before becoming a foreign trust, all of its assets to a foreign trust.”

(2) EFFECTIVE DATE.—The amendment made by this subsection shall take effect on the date of the enactment of this Act.

I. INTRODUCTION

A. Purpose and Summary

H.R. 3286, as amended and reported by the Committee on Ways and Means, provides: (1) a tax credit for certain adoption expenses and an exclusion for amounts received by an employee for certain adoption expenses under an employer adoption assistance program (Title I); (2) removal of barriers to interethnic adoptions (Title II); and (3) revenue offsets for the bill (repeal of business exclusion for energy subsidies provided by public utilities and modification of foreign trust rules) (Title IV). The Committee on Ways and Means acted only on Titles I, II, and IV of the bill. Title III (relating to child custody proceedings affected by the Indian Child Welfare Act of 1978) was referred to the Committee on Resources, which struck Title III of the bill on April 25, 1996 (see H. Rept. 104–542, Part 1, April 30, 1996). Title II also was referred to the Committee on Economic and Educational Opportunities, which was discharged on April 30, 1996.

B. Background and Need for Legislation

Adoption in the United States is too rare. One of the most troubling demographic trends in recent decades is the increasing number of children living apart from their biological parents, primarily in foster homes. The best available information indicates that about 450,000 children live in foster care at any given moment, and as many as 600,000 live in foster care during the course of a given year. Both figures appear to be rising slightly after more rapid growth during the late 1980s.

The Committee on Ways and Means, which has jurisdiction over many of the major Federal programs designed to address the problem of family dissolution, has a long history of taking decisive action to help these children. Federal programs under Committee jurisdiction now provide well over \$5 billion per year to support foster care, adoption, and family services. Based on evidence presented to the Committee in recent years through testimony, letters, and various reports, the Committee has determined that a major goal of Federal policy must be the promotion of adoption. This legislation was designed to address two of the major barriers to adoption: the cost to families of adopting a child and the practice of requiring adopting parents and the adopted child to be of the same race or color.

Adoption costs now constitute a major disincentive to adoption, especially for moderate-income families. Given that adoption expenses can total \$10,000 to \$15,000 or even more in some cases, the Committee designed a tax credit to help families defray these expenses. The bill provides a nonrefundable tax credit for up to

\$5,000 for qualified adoption expenses and an exclusion of up to \$5,000 for amounts received by an employee for qualified adoption expenses under an employer adoption assistance program. Both the tax credit and the exclusion are phased out for taxpayers with modified adjusted gross income above \$75,000. The \$5,000 maximums are per child adopted. These provisions will assist families that need financial assistance in adopting children.

The bill also is intended to remove bureaucratic barriers to inter-ethnic adoptions by providing that not later than January 1, 1997, States receiving funds from the Federal Government for adoption or foster care placements may not deny any person the opportunity to become an adoptive or foster parent on the basis of race, color, or national origin of the person or of the child, nor may the State delay or deny the placement of a child for adoption or into foster care on the basis of race, color, or national origin of the adoptive or foster parent or of the child. Recent studies show that many States allow the use of race in the placement of children in foster care and adoption, which has resulted in minority children remaining in foster care at least twice as long as non-minority children.

Finally, the bill includes two revenue offsets to pay for the other provisions of the bill: (1) repeal of the business exclusion for energy subsidies provided by public utilities; and (2) modification of the foreign trust rules to improve compliance.

C. Legislative History

Committee Bill

H.R. 3286 was introduced on April 23, 1996, by Ms. Molinari and Messrs. Archer and Bunning, Ms. Pryce, and Messrs. Solomon, Tiahrt, and Shaw. The bill was amended in a Committee markup on May 1, 1996. The bill, as amended, was ordered favorably reported by the Committee on Ways and Means by a voice vote on May 1, 1996.

An amendment by Mr. Jacobs, to the pending Rangel amendment restoring current law language regarding the use of cultural, ethnic or racial considerations in placement of children into foster care or adoptive homes, to clarify that the Rangel amendment was not intended to result in continued foster care of the child, was approved by unanimous consent. The Rangel amendment, as amended, was defeated by a roll call vote of 15 yeas to 22 nays.

An amendment by Mr. Shaw to strike the phrase "or otherwise discriminate in making a placement decision" on pages 10 (lines 9–11) and 12 (lines 10–11) of the introduced bill was approved by unanimous consent.

An amendment by Chairman Archer to clarify the provisions of Title IV relating to treatment of foreign trusts was approved by unanimous consent.

A provision similar to the interethnic adoption provision in H.R. 3286 was approved by the Committee on March 8, 1995, as part of H.R. 4, the Welfare Transformation Act of 1995. That provision was subsequently incorporated into both the Balanced Budget Act of 1995 (H.R. 2491) and the Personal Responsibility and Work Opportunity Act of 1995 (H.R. 4), both of which were passed by Congress but vetoed by President Clinton.

Provisions similar to the Title I adoption tax credit were approved by the Committee as part of H.R. 1215 (Contract With America Tax Relief Act of 1995) on March 14, 1995 (H. Rept. 104–84). These provisions were also incorporated into the vetoed Balanced Budget Act of 1995, H.R. 2491 (see H. Rept. 104–350 for the conference report). In addition, provisions similar to the Title IV revenue-offset provisions (repeal of the business exclusion for energy subsidies provided by public utilities and modification of the foreign trust rules) were included in the vetoed H.R. 2491.

Legislative Hearings

The Subcommittee on Human Resources of the Committee on Ways and Means held a joint hearing on child care and child welfare with the Subcommittee on Children, Youth, and Families of the Committee on Economic and Educational Opportunities on February 3, 1995. In addition, the Subcommittee on Human Resources held a Federal adoption policy hearing on May 10, 1995. Also, the Committee held hearings on January 17–18, 1995, on “Contract With America” tax proposals relating to the family—including a tax credit for adoption expenses.

II. EXPLANATION OF THE BILL

A. Tax Credit for Adoption Expenses; Exclusion for Certain Adoption Expenses (sec. 101 of the bill and new secs. 23 and 137 of the Code)

Present Law

Present law does not provide a tax credit for adoption expenses. Also, present law does not provide an exclusion from gross income for employer-provided adoption assistance. The Federal Adoption Assistance program (a Federal outlay program) provides financial assistance for the adoption of certain special needs children. In general, a special needs child is defined as a child who (1) according to a State determination, could not or should not be returned to the home of the birth parents and (2) on account of a specific factor or condition (such as ethnic background, age, membership in a minority or sibling group, medical condition, or physical, mental or emotional handicap), could not reasonably be expected to be adopted unless adoption assistance is provided. Specifically, the program provides assistance for adoption expenses for those special needs children receiving Federally assisted adoption assistance payments as well as special needs children in private and State-funded programs. The maximum Federal reimbursement is \$1,000 per special needs child. Reimbursable expenses include those non-recurring costs directly associated with the adoption process such as legal costs, social service review, and transportation costs.

Reasons for Change

The Committee believes that the financial costs of the adoption process should not be a barrier to adoptions. In addition, the Committee wishes to encourage further the adoption of special needs children. Therefore the tax credit is allowed in addition to any

grant money received for the adoption expenses associated with the adoption of special needs children.

Explanation of Provision

Tax credit

The bill provides taxpayers with a maximum nonrefundable credit against income tax liability of \$5,000 per child for qualified adoption expenses paid or incurred by the taxpayer. Qualified adoption expenses are reasonable and necessary adoption fees, court costs, attorneys' fees and other expenses that are directly related to the legal adoption of an eligible child. In the case of an international adoption, the credit is not available unless the adoption is finalized. In that case the credit is allowed for all prior qualified expenses in the year that the adoption becomes final. An eligible child is an individual (1) who has not attained age 18 as of the time of the adoption, or (2) who is physically or mentally incapable of caring for himself or herself. No credit is allowed for expenses incurred (1) in violation of State or Federal law, (2) in carrying out any surrogate parenting arrangement, or (3) in connection with the adoption of a child of the taxpayer's spouse. The credit is phased out ratably for taxpayers with modified adjusted gross income (AGI) above \$75,000, and is fully phased out at \$115,000 of modified AGI. For these purposes modified AGI is computed by increasing the taxpayer's AGI by the amount otherwise excluded from gross income under Code sections 911, 931, or 933 (relating to the exclusion of income of U.S. citizens or residents living abroad; residents of Guam, American Samoa, and the Northern Mariana Islands, and residents of Puerto Rico, respectively).

The \$5,000 limit is a per child limit, not an annual limitation. For example, in the case of a domestic adoption if a taxpayer pays or incurs \$3,000 of otherwise allowable qualified adoption expenses with respect to a child in year one and \$3,000 of otherwise allowable qualified adoption expenses with respect to that same child in year two, then the taxpayer would receive a \$3,000 credit with respect to year one and a \$2,000 credit with respect to year two. The credit may be less than \$5,000 because of other limitations. It is also intended that when more than one taxpayer pays or incurs qualified adoption expenses for the adoption of the same child the total adoption credit claimed by all parties shall not exceed \$5,000.

To avoid a double benefit, the bill denies the credit to taxpayers to the extent the taxpayer may use otherwise qualified adoption expenses as the basis of another credit or deduction. Also, when the adoption credit is allowed because the taxpayer expends amounts chargeable to a capital account (e.g., the costs of constructing a ramp at the taxpayer's house to accommodate a wheelchair that is required as a condition of the adoption) the taxpayer is not allowed additional basis in the house to the extent of the adoption credit allowed. Where the amount of qualified adoption expenses exceeds \$5,000, (e.g., \$5,000 of legal fees and \$5,000 of ramp construction costs) it is intended that the amounts not chargeable to a capital account (the legal fees) are treated as the basis of the credit before any amounts that are chargeable to a capital account. In this way the taxpayer may satisfy the requirements of the adoption credit

with the legal fees and may add the ramp construction costs to the basis in the house.

The credit is not allowed for any expenses for which a grant is received under any Federal, State, or local program. This latter limit, however, does not apply in the case of special needs adoptions. A special needs child is a child who the State has determined: (1) cannot or should not be returned to the home of the birth parents, and (2) has a specific factor or condition because of which the child cannot be placed with adoptive parents without adoption assistance. Examples of factors or conditions are the child's ethnic background, age, membership in a minority or sibling group, medical conditions, or physical, mental, or emotional handicaps.

The bill provides that individuals who are married at the end of the taxable year must file a joint return to receive the credit unless they lived apart from each other for the last six months of the taxable year and the individual claiming the credit (1) maintained as his or her home a household for the child for more than one-half of the taxable year and (2) furnished over one-half of the cost of maintaining that household in that taxable year. Further, the bill provides that an individual legally separated from his spouse under a decree of divorce or separate maintenance would not be considered married for purposes of this provision.

The bill provides that to the extent the otherwise allowable credit exceeds the tax liability limitation of section 26 (reduced by other personal credits) the excess shall be carried forward as an adoption credit into the next taxable year, up to a maximum of five taxable years.

Exclusion from income

The bill provides a maximum \$5,000 exclusion from the gross income of an employee for qualified adoption expenses paid by the employer. The \$5,000 limit is a per child limit, not an annual limitation. Also, the total exclusion allowed to two or more taxpayers with respect to the adoption of the same child may not exceed \$5,000. In order for the exclusion to apply, the expenses have to be paid under an adoption assistance program in connection with an adoption of an eligible child (as described above) by an employee. An adoption assistance program is a nondiscriminatory plan of an employer under which the employer provides employees with adoption assistance. Also, not more than five percent of the benefits under the program for any year can benefit a class of individuals consisting of more than five-percent owners of the employee or their spouses or dependents. An adoption assistance program does not have to be funded. An adoption reimbursement program operated under section 1052 of title 10 of the U.S. Code (relating to the armed forces) or section 514 of title 14 of the U.S. Code (relating to members of the Coast Guard) is treated as an adoption assistance program for these purposes. Adoption assistance is a qualified benefit under a cafeteria plan. The exclusion is phased out ratably for taxpayers with modified AGI above \$75,000 and is fully phased out at \$115,000 of modified AGI. In the case of expenses paid under an adoption assistance program that may otherwise be

chargeable to a capital account, an ordering rule similar to the one for the adoption credit applies.

Adoption expenses paid or reimbursed under an adoption assistance program may not be taken into account in determining the adoption credit. A taxpayer may, however, satisfy the requirements of the adoption credit and exclusion with different expenses paid or incurred by the taxpayer and employer respectively. For example in the case of an adoption that costs \$10,000 with \$5,000 of expenses paid by the taxpayer and \$5,000 paid by the taxpayer's employer under an adoption assistance program the taxpayer may qualify for the adoption credit and the exclusion.

Taxpayer identification numbers (TINS)

The Committee is concerned that problems may arise in processing tax returns of adopting parents because of unavoidable delays involved in obtaining a social security number of a child who is being adopted. The Committee understands that the Internal Revenue Service recognizes these concerns and is committed to working with the Committee to develop as soon as possible an administrative solution that minimizes the burdens imposed on adopting parents while balancing processing and potential compliance considerations.

Effective Date

The provision is effective for taxable years beginning after December 31, 1996.

B. Removal of Barriers to Interethnic Adoption

(Sec. 201 of the bill and secs. 471(a) and 474 of the Social Security Act)

Present Law

State law governs adoption and foster care placement. Many States permit race matching of foster and adoptive parents with children either in regulation, statute, policy, or practice. The Howard M. Metzenbaum Multiethnic Placement Act of 1994 ("Metzenbaum Act", Public Law 103-382) permits States to consider race and ethnicity in selecting a foster care or adoptive home, but States cannot delay or deny the placement of the child solely on the basis of race, color or national origin.

Noncompliance with the Metzenbaum Act is deemed a violation of Title VI of the Civil Rights Act of 1964.

Reasons for Change

Various hearings and numerous letters led the Committee to conclude that Public Law 103-382 was not having the intended effect of facilitating the adoption of minority children. The Committee concluded that the legislative language was internally inconsistent. On the one hand, it prohibited any agency or state entity that receives Federal assistance from delaying or denying the placement of a child for adoption or into foster care solely on the basis of the race, color or national origin of the adoptive or foster parents. On the other hand, it also allowed placement agencies to use "cultural, ethnic or racial background of the child" as criteria in making

placement decisions. In addition, Public Law 103-382 lacked an enforcement provision backed by serious penalties. As a result, the bill was ineffective in promoting the best interests of children by decreasing the length of time they wait to be adopted.

Under the terms of the Committee bill, "race, color or national origin" cannot be used to delay or deny the placement of a child into a foster or adoptive placement. The Committee agreed that any delay is clearly not in the child's best interest and must not be tolerated for the purposes of race-matching. The major concern of the Committee is to ensure that States that can be shown to pursue policies that lead to any delay in the adoption of any child be subjected to the penalty terms of this legislation.

Explanation of Provision

Section 553 of the Metzenbaum Act is repealed. In addition, Section 471 of the Social Security Act is amended to prohibit a State or other entity that receives Federal assistance from denying to any person the opportunity to become an adoptive or a foster parent on the basis of the race, color, or national origin of the person or of the child involved. Similarly, no State or other entity receiving Federal funds can delay or deny the placement of a child for adoption or foster care, or otherwise discriminate in making a placement decision, on the basis of the race, color, or national origin of the adoptive or foster parent or the child involved.

Section 474 of the Social Security Act is amended to require the Secretary to reduce the amount of Federal foster care and adoption funds provided to the State through Title IV-E if the State program is found in violation of this provision as a result of a review conducted under Section 1123 of the Social Security Act. States found to be in violation would have their quarterly funds reduced by 2 percent for the first violation, by 5 percent for the second violation, and by 10 percent for the third or subsequent violation.

Private entities found to be in violation of this provision for a quarter are required to return to the Secretary all federal funds received from the State during the quarter.

Any individual who is harmed by a violation of this provision may seek redress in any United States district court. An action under this provision may not be brought more than two years after the alleged violation occurred.

Noncompliance with this provision constitutes a violation of Title VI of the Civil Rights Act of 1964. The Indian Child Welfare Act of 1978 is not affected by changes made in this title.

Effective Date

The effective date for this provision is upon enactment (except States must meet the State plan requirement provision of bill section 201(a) not later than January 1, 1997).

C. Revenue Offsets

1. Remove business exclusion for energy subsidies provided by public utilities (sec. 401 of the bill and sec. 136 of the Code)

Present Law

Internal Revenue Code section 136, as added by the Energy Policy Act of 1992, provides an exclusion from the gross income of a customer of a public utility for the value of any subsidy provided by the utility for the purchase or installation of an energy conservation measure with respect to a dwelling unit (as defined by sec. 280A(f)(1)). In addition, for subsidies received after 1994, section 136 provides a partial exclusion from gross income for the value of any subsidy provided by a utility for the purchase or installation of an energy conservation measure with respect to property that is not a dwelling unit. The amount of the exclusion is 40 percent of the value for subsidies received in 1995, 50 percent of the value for subsidies received in 1996, and 65 percent of the value for subsidies received after 1996.

For this purpose, an energy conservation measure is any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to property. With respect to property other than a dwelling unit, an energy conservation measure includes “specially defined energy property” (generally, property described in sec. 48(l)(5) of the Code as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990).

The exclusion does not apply to payments made to or from a qualified cogeneration facility or a qualifying small power production facility pursuant to section 210 of the Public Utility Regulatory Policy Act of 1978.

Section 136 denies a deduction or credit to a taxpayer (or in appropriate cases requires a reduction in the adjusted basis of property of a taxpayer) for any expenditure to the extent that a subsidy related to the expenditure was excluded from the gross income of the taxpayer.

Reasons for Change

The Committee believes that the present-law exclusion for energy conservation subsidies results in the mismeasurement of income and may create biases against certain types of conservation programs. However, the Committee believes the exclusion is appropriate for individual consumers because the taxation of such benefits may impose unduly harsh recordkeeping burdens with respect to these taxpayers. Thus, the bill only repeals the exclusion for subsidies with respect to nonresidential property.

Explanation of Provision

The bill repeals the partial exclusion for any subsidy provided by a utility for the purchase or installation of an energy conservation measure with respect to property that is not a dwelling unit.

Effective Date

The provision is effective for subsidies received after December 31, 1996, unless received pursuant to a binding written contract in effect on September 13, 1995, and all times thereafter.

- 2. Modify treatment of foreign trusts (secs. 411–417 of the bill and secs. 643, 665, 668(a), 672, 679, 1491, 1494, 6038, 6039G, 6677, 7701(a) and 7872(f) of the Code)**

Present Law

Inbound grantor trusts with foreign grantors

Under the grantor trust rules (secs. 671–679), a grantor that retains certain rights or powers generally is treated as the owner of the trust's assets without regard to whether the grantor is a domestic or foreign person. Under these rules, U.S. trust beneficiaries are not subject to U.S. tax on distributions from a trust where a foreign grantor is treated as owner of the trust, even though no tax may be imposed on the trust income by any jurisdiction. In addition, a special rule provides that if a U.S. beneficiary of an inbound grantor trust transfers property to the foreign grantor by gift, that U.S. beneficiary is treated as the grantor of the trust to the extent of the transfer.

Foreign trusts that are not grantor trusts

Under the accumulation distribution rules (which generally apply to distributions from a trust in excess of the trust's distributable net income for the taxable year), a distribution by a foreign nongrantor trust of previously accumulated income generally is taxed at the U.S. beneficiary's average marginal rate for the prior 5 years, plus interest (secs. 666 and 667). Interest is computed at a fixed annual rate of 6 percent, with no compounding (sec. 668). If adequate records of the trust are not available to determine the proper application of the rules relating to accumulation distributions to any distribution from a trust, the distribution is treated as an accumulation distribution out of income earned during the first year of the trust (sec. 666(d)).

If a foreign nongrantor trust makes a loan to one of its beneficiaries, the principal of such a loan generally is not taxable as income to the beneficiary.

Outbound foreign grantor trusts with U.S. grantors

Under the grantor trust rules, a U.S. person that transfers property to a foreign trust generally is treated as the owner of the portion of the trust comprising that property for any taxable year in which there is a U.S. beneficiary of any portion of the trust (sec. 679(a)). This treatment generally does not apply, however, to transfers by reason of death, to transfers made before the transferor became a U.S. person, or to transfers that represent sales or exchanges of property at fair market value where gain is recognized to the transferor.

Residence of trusts

A trust is treated as foreign if it is not subject to U.S. income taxation on its income that is neither derived from U.S. sources nor effectively connected with the conduct of a U.S. trade or business. Thus, if a trust is taxed in a manner similar to a nonresident alien individual, it is considered to be a foreign trust. Any other trust is treated as domestic.

Section 1491 generally imposes a 35-percent excise tax on a U.S. person that transfers appreciated property to certain foreign entities, including a foreign trust. In the case of a domestic trust that changes its situs and becomes a foreign trust, it is unclear whether property has been transferred from a U.S. person to a foreign entity and, thus, whether the transfer is subject to the excise tax.

Information reporting and penalties related to foreign trusts

Any U.S. person that creates a foreign trust or transfers money or property to a foreign trust is required to report that event to the Treasury Department without regard to whether the trust is a grantor trust or a nongrantor trust. Similarly, any U.S. person that transfers property to a foreign trust that has one or more U.S. beneficiaries is required to report annually to the Treasury Department. In addition, any U.S. person that makes a transfer described in section 1491 is required to report the transfer to the Treasury Department.

Any person that fails to file a required report with respect to the creation of, or a transfer to, a foreign trust may be subject to a penalty of 5 percent of the amount transferred to the foreign trust. Similarly, any person that fails to file a required annual report with respect to a foreign trust with U.S. beneficiaries may be subject to a penalty of 5 percent of the value of the corpus of the trust at the close of the taxable year. The maximum amount of the penalty imposed under either case may not exceed \$1,000. A reasonable cause exception is available.

Reporting of foreign gifts

There is no requirement to report gifts or bequests from foreign sources.

Reasons for Change***Grantor trust rules******Inbound grantor trusts***

The Committee has been informed that the U.S. grantor trust provisions are being used as a vehicle to avoid U.S. tax. If a trust is treated as a grantor trust, only the owner of the trust is taxable on the trust's income and not the trust's beneficiaries. Thus, if a foreign person creates a trust with U.S. beneficiaries that is treated as a grantor trust for U.S. tax purposes and if the foreign person's home country does not tax the income, the income of the trust would not be subject to tax by either the United States or the foreign country. The Committee believes that the income derived through these types of arrangements should be subject to tax by at least one jurisdiction.

Outbound grantor trusts

The Committee understands that taxpayers have avoided the application of the outbound grantor trust rules of section 679. For example, a transfer of property to a foreign trust may be structured as a sale in exchange for a note issued by the trust or a person related to the trust where the note will not be repaid. The Committee believes that it is appropriate to disregard notes that do not reflect arm's-length terms in determining whether the transferor received fair market value for the property transferred.

Foreign nongrantor trust rules

The 6-percent simple interest charge applicable to accumulation distributions has not been updated since 1976. In essence, income earned through a foreign nongrantor trust may be deferred from U.S. taxation, then subjected to a below-market interest rate when distributed to a U.S. beneficiary. The Committee believes that it is appropriate to charge the same rate of interest on accumulation distributions as is applicable to general underpayments of income tax.

Under current law, a U.S. beneficiary of a foreign trust may avoid U.S. tax on the income accumulated through the trust by obtaining a "loan" of cash or marketable securities from the trust in lieu of an actual distribution. The Committee believes that it is appropriate to treat loans that do not reflect arm's-length terms as distributions to the borrower.

Residence of trusts

Because the U.S. tax treatment of a trust (and the beneficiaries of a trust) depends on the residence of the trust, the Committee believes that it is appropriate to provide objective criteria for determining the residence of trusts.

Information reporting requirements and associated penalties

The Committee has been informed that certain U.S. settlors have established foreign trusts, including grantor trusts, in tax haven jurisdictions. Income from such foreign grantor trusts is taxable currently to the U.S. grantor, but the Committee understands that there is noncompliance in this regard. The Committee is concerned that the present-law civil penalties for failure to comply with the reporting requirements applicable to foreign trusts established by U.S. persons have proven to be ineffective. In order to deter noncompliance, the Committee believes that it is appropriate to expand the reporting requirements relating to activities of foreign trusts with U.S. grantors or U.S. beneficiaries and to increase the civil penalties applicable to a failure to comply with such reporting requirements.

The Committee understands that some of the jurisdictions in which U.S. settlors have established foreign trusts have strict secrecy laws. The Committee is concerned that the secrecy laws may effectively preclude the Treasury Department from obtaining information necessary to determine the tax liabilities of the U.S. grantors or U.S. beneficiaries with respect to items related to such foreign trusts. The Committee believes that, it is useful, in the case of a foreign trust with a U.S. grantor, to provide an incentive for

the trust to have a limited U.S. agent to accept service of process in order to improve the administrability of the tax law applicable to taxation of income derived from foreign trusts.

Explanation of Provisions

Overview

The bill modifies the tax treatment of trusts as follows:

a. The grantor trust rules generally apply only to the extent that they result, directly or indirectly, in income or other amounts (if any) being currently taken into account in computing the income of a U.S. person. Certain exceptions apply.

b. Beginning on January 1, 1996, the interest rate applicable to accumulation distributions from foreign nongrantor trusts is the rate imposed on underpayment of tax under section 6621(a)(2), with compounding. The accumulation distribution generally is allocated proportionately to prior trust years in which the trust had undistributed net income. The full amount of a loan of cash or marketable securities by a foreign nongrantor trust to a U.S. grantor or a U.S. beneficiary (or a U.S. person related to such a grantor or beneficiary) generally is treated as a distribution to the grantor or beneficiary.

c. A nonresident alien who transfers property to a foreign trust and then becomes a U.S. resident within 5 years after the transfer is treated as making a transfer to the foreign trust on his residency starting date. In determining whether a foreign trust paid fair market value to the transferor for property transferred to the trust, obligations issued by the trust, by any grantor or beneficiary of the trust, or by any person related to any grantor or beneficiary generally are not taken into account.

d. The bill authorizes the Secretary of the Treasury to issue regulations to prevent abusive transactions to avoid the purposes of these rules.

e. A two-part objective test is established for determining whether a trust is foreign or domestic for tax purposes.

f. The bill expands the reporting requirements with respect to foreign trusts if there is a U.S. grantor of the foreign trust or a distribution from the foreign trust to a U.S. person. The bill requires the responsible parties to file information returns with the Treasury Department upon the occurrence of certain events. A failure to comply with the reporting requirements results in increased monetary penalties. Special sanctions apply unless a U.S. owner of any portion of a foreign trust appoints a limited agent to accept service of process with respect to requests and summons by the Treasury Department in connection with the tax treatment of items relating to the trust.

g. Any U.S. person (other than certain tax-exempt organizations) that receives purported gifts or bequests from foreign sources totaling more than \$10,000 during the year is required to report the gift to the Treasury Department. Monetary penalties and other sanctions apply to a failure to comply with the reporting requirement.

The provisions are described in more detail below.

a. Inbound grantor trusts with foreign grantors

Foreign grantors not treated as owners

Under the bill, the grantor trust rules generally apply only to the extent that they result, directly or indirectly, in income or other amounts (if any) being currently taken into account in computing the income of a U.S. citizen or resident or a domestic corporation. Thus, the grantor trust rules generally do not apply to any portion of a trust where their effect is to treat a foreign person as owner of that portion.

The bill provides certain exceptions to the rule described above. Under one exception, the grantor trust rules continue to apply to the portion of a trust where that portion of the trust is revocable by the grantor either without approval of another person or with the consent of a related or subordinate party who is subservient to the grantor (as defined in sec. 672(c)). Under another exception, the grantor trust rules continue to apply to the portion of a trust where the only amounts distributable from that portion during the lifetime of the grantor are to the grantor or the grantor's spouse. The general rule denying grantor trust status does not apply to trusts established to pay compensation, and certain trusts in existence as of September 19, 1995 provided that such trust is treated as owned by the grantor under section 676 or 677 (other than sec. 677(a)(3)).¹ In addition, the grantor trust rules generally apply where the grantor is a controlled foreign corporation (as defined in sec. 957). Finally, the grantor trust rules continue to apply in determining whether a foreign corporation is characterized as a passive foreign investment company ("PFIC"). Thus, a foreign corporation cannot avoid PFIC status by transferring its assets to a grantor trust.

If a U.S. beneficiary, or a family member of such a beneficiary,² of an inbound grantor trust transfers property to the foreign grantor, such beneficiary generally is treated as a grantor of a portion of the trust to the extent of the transfer. This rule applies without regard to whether the foreign grantor is otherwise treated as the owner of any portion of such trust. However, this rule does not apply if the transfer is a sale of the property for full and adequate consideration or if the transfer is a gift that qualifies for the annual exclusion described in section 2503(b).

The bill provides a special rule that allows the Secretary of the Treasury to recharacterize a transfer, directly or indirectly, from a partnership or foreign corporation which the transferee treats as a gift or bequest, to prevent the avoidance of the purpose of section 672(f).³

In a case where a foreign person (that would be treated as the owner of a trust but for the above rule) actually pays tax on the income of the trust to a foreign country, the Committee anticipates that Treasury regulations will provide that, for foreign tax credit purposes, U.S. beneficiaries that are subject to U.S. income tax on the same income will be treated as having paid the foreign taxes

¹ The exception does not apply to the portion of any such trust attributable to any transfers made after September 19, 1995.

² For this purpose, a family member is generally defined as a brother, sister, spouse, ancestor or lineal descendant.

³ See discussion below for reporting requirements under the bill with respect to certain foreign gifts and bequests received by a U.S. person.

that are paid by the foreign grantor. Any resulting foreign tax credits would be subject to applicable foreign tax credit limitations.

The bill provides a transition rule for any domestic trust that has a foreign grantor that is treated as the owner of the trust under present law, but becomes a nongrantor trust under the bill. If such a trust becomes a foreign trust before January 1, 1997, or if the assets of such a trust are transferred to a foreign trust before that date, such trust is exempt from the excise tax on transfers to a foreign trust otherwise imposed by section 1491. However, the bill's new reporting requirements and penalties are applicable to such a trust and its beneficiaries. In addition, the assets of such a trust will be treated as if they were recontributed to a nongrantor trust by the foreign grantor, with no recognition of gain or loss, on the date the trust ceases to be treated as a grantor trust. The nongrantor trust will have the same basis in such assets as did the grantor on the date the trust ceases to be treated as a grantor trust.

Distributions by foreign trusts through nominees

The bill generally treats any amount paid to a U.S. person, where the amount was derived (directly or indirectly) from a foreign trust, as if paid by the foreign trust directly to the U.S. person. This rule disregards the role of an intermediary or nominee that may be interposed between a foreign trust and a U.S. beneficiary. Unlike present law, however, the rule applies whether or not the trust was created by a U.S. person. The rule does not apply to a withdrawal from a foreign trust by its grantor, with a subsequent gift or other payment to a U.S. person.

Effective date

The provisions discussed in this part are effective on the date of enactment.

b. Foreign trusts that are not grantor trusts

Interest charge on accumulation distributions

The bill changes the interest rate applicable to accumulation distributions from foreign trusts from simple interest at a fixed rate of 6 percent to compound interest determined in the same manner as interest imposed on underpayments of tax under section 6621(a)(2). Simple interest is accrued at the rate of 6 percent through 1995. Beginning on January 1, 1996, however, compound interest based on the underpayment rate is imposed not only on tax amounts determined under the accumulation distribution rules but also on the total simple interest for pre-1996 periods, if any. For purposes of computing the interest charge, the accumulation distribution is allocated proportionately to prior trust years in which the trust has undistributed net income (and the beneficiary receiving the distribution was a U.S. citizen or resident), rather than to the earliest of such years. An accumulation distribution is treated as reducing proportionately the undistributed net income from prior years.

The bill includes a formula to determine the period for which interest is charged using the underpayment rates under section

6621(a)(2). Under the formula, for example, if a foreign nongrantor trust had \$100 of undistributed net income each year in years 1 through 3 and the trust distributes \$100 of accumulated income to its U.S. beneficiary in year 4, the taxpayer has to pay interest using the section 6621(a)(2) interest rates as if the income accrued for 2 years.⁴ In addition, the \$100 accumulation distribution reduces the trust's undistributed net income by \$33 each year for years 1 through 3.⁵

Loans to grantors or beneficiaries

In the case of a loan of cash or marketable securities by the foreign trust to a U.S. grantor or a U.S. beneficiary (or a U.S. person related to such grantor or beneficiary⁶), except to the extent provided by Treasury regulations, the bill treats the full amount of the loan as distributed to the grantor or beneficiary. The Committee expects that the Treasury regulations will provide an exception from this treatment for loans with arm's-length terms. In applying this exception, the Committee further expects consideration to be given to whether there is a reasonable expectation that a loan will be repaid. In addition, any subsequent transaction between the trust and the original borrower regarding the principal of the loan (e.g., repayment) is disregarded for all purposes of the Code. This provision does not apply to loans made to persons that are exempt from U.S. income tax.

Effective date

The provision to modify the interest charge on accumulation distributions applies to distributions after the date of enactment. The provision with respect to loans to U.S. grantors, U.S. beneficiaries or a related U.S. person related to such a grantor or beneficiary applies to loans made after September 19, 1995.

c. Outbound foreign grantor trusts with U.S. grantors

The bill makes several modifications to the general rule of section 679(a)(1) under which a U.S. person who transfers property to a foreign trust generally is treated as the owner of the portion of the trust comprising that property for any taxable year in which there is a U.S. beneficiary of the trust. The bill also contains an amendment to conform the definition of certain foreign corporations the income of which is deemed to be accumulated for the benefit of a U.S. beneficiary to the definition of controlled foreign corporations (as defined in sec. 957(a)).

Sale or exchange at market value

Present law contains several exceptions to grantor trust treatment under section 679(a)(1) described above. Under one of the exceptions, grantor trust treatment does not result from a transfer of

⁴The number of years is determined as a weighted average as follows: $(\$100 \times 3 \text{ years}) + (\$100 \times 2 \text{ years}) + (\$100 \times 1 \text{ year}) \div \$300 = 2$

⁵That is, one-third of the \$100 of distribution reduces the \$100 of undistributed net income for each of years 1, 2 and 3.

⁶For this purpose, a person generally would be treated as related to the grantor or beneficiary if the relationship between such person and the grantor or beneficiary would result in a disallowance of losses under section 267 or 707(b), except that in applying section 267(c)(4) an individual's family includes the spouses of the members of the family.

property by a U.S. person to a foreign trust in the form of a sale or exchange at fair market value where gain is recognized to the transferor. In determining whether the trust paid fair market value to the transferor, the bill provides that obligations issued (or, to the extent provided by regulations, guaranteed) by the trust, by any grantor or beneficiary of the trust, or by any person related to any grantor or beneficiary⁷ (referred to as “trust obligations”) generally are not taken into account except as provided in Treasury regulations. The Committee expects that the Treasury regulations will provide an exception from this treatment for loans with arm’s-length terms. In applying this exception, the Committee further expects consideration to be given to whether there is a reasonable expectation that a loan will be repaid. Principal payments by the trust on any such trust obligations generally will reduce the portion of the trust attributable to the property transferred (i.e., the portion of which the transferor is treated as the grantor).

Other transfers

The bill adds a new exception to the general rule of section 679(a)(1) described above. Under the bill, a transfer of property to certain charitable trusts is exempt from the application of the rules treating foreign trusts with U.S. grantors and U.S. beneficiaries as grantor trusts.

Transferors or beneficiaries who become U.S. persons

The bill applies the rule of section 679(a)(1) to certain foreign persons who transfer property to a foreign trust and subsequently become U.S. persons. A nonresident alien individual who transfers property, directly or indirectly, to a foreign trust and then becomes a resident of the United States within 5 years after the transfer generally is treated as making a transfer to the foreign trust on the individual’s U.S. residency starting date (as defined in sec. 7701(b)(2)(A)). The amount of the deemed transfer is the portion of the trust (including undistributed earnings) attributable to the property previously transferred. Consequently, the individual generally is treated under section 679(a)(1) as the owner of that portion of the trust in any taxable year in which the trust has U.S. beneficiaries. The bill’s reporting requirements and penalties (discussed below) also are applicable.

Under the bill, a beneficiary is not treated as a U.S. person for purposes of determining whether the transferor of property to a foreign trust is taxed as a grantor with respect to any portion of a foreign trust if such beneficiary first became a U.S. person more than 5 years after the transfer.

Outbound trust migrations

The bill applies the rules of section 679(a)(1) to a U.S. person that transferred property to a domestic trust if the trust subsequently becomes a foreign trust while the transferor is still alive. Such a person is deemed to make a transfer to the foreign trust

⁷For this purpose, a person is treated as related to the grantor or beneficiary if the relationship between such person and the grantor or beneficiary would result in a disallowance of losses under section 267 or 707(b), except that in applying section 267(c)(4) an individual’s family includes the spouses of the members of the family.

on the date of the migration. The amount of the deemed transfer is the portion of the trust (including undistributed earnings) attributable to the property previously transferred. Consequently, the individual generally is treated under the rules of section 679(a)(1) as the owner of that portion of the trust in any taxable year in which the trust has U.S. beneficiaries. The bill's reporting requirements and penalties (discussed below) also are applicable.

Effective date

The provisions to amend section 679 apply to transfers of property after February 6, 1995.

d. Anti-abuse regulatory authority

In general

The bill includes an anti-abuse rule which authorizes the Secretary of the Treasury to issue regulations, on or after the date of enactment, that may be necessary or appropriate to carry out the purposes of the rules applicable to estates, trusts and beneficiaries, including regulations to prevent the avoidance of those purposes.

Effective date

The provision is effective on the date of enactment.

e. Residence of trusts

Treatment as U.S. person

The bill establishes a two-part objective test for determining for tax purposes whether a trust is foreign or domestic. If both parts of the test are satisfied, the trust is treated as domestic.

Under the first part of the proposed test, in order for a trust to be treated as domestic, a U.S. court (i.e., Federal, State, or local) must be able to exercise primary supervision over the administration of the trust. The Committee expects that this test generally will be satisfied by any trust instrument that specifies that it is to be governed by the laws of any State.

Under the second part of the proposed test, in order for a trust to be treated as domestic, one or more U.S. fiduciaries must have the authority to control all substantial decisions of the trust. The Committee expects that this test will be satisfied in any case where fiduciaries that are U.S. persons hold a majority of the fiduciary power (whether by vote or otherwise), and where no foreign fiduciary, such as a "trust protector" or other trust advisor, has the power to veto important decisions of the U.S. fiduciaries. The Committee further expects that, in applying this test, a reasonable period of time will be allowed for a trust to replace a U.S. fiduciary that resigns or dies before the trust is treated as foreign.

Under the bill, a foreign trust is defined as a trust other than a trust that is determined to be domestic under both the court-supervision test and the U.S. fiduciary test.

Outbound migration of domestic trusts

Under the bill, if a domestic trust changes its situs and becomes a foreign trust, the trust is treated as having made a transfer of its assets to a foreign trust and is subject to the 35-percent excise

tax imposed by present-law section 1491 unless one of the exceptions to this excise tax is applicable. The U.S. grantor also is required to report the transfer under the reporting requirements described below. Failure to report such a transfer would result in penalties (discussed below).

Effective date

The provision to modify the treatment of a trust as a U.S. person applies to taxable years beginning after December 31, 1996. In addition, if the trustee of a trust so elects, the provision would apply to taxable years ending after the date of enactment. The amendment to section 1491 is effective on the date of enactment.

f. Information reporting and penalties relating to foreign trusts

The bill expands the reporting requirements with respect to foreign trusts if there is a U.S. grantor of the foreign trust or a distribution from the foreign trust to a U.S. person. The bill requires the responsible parties to file information returns with the Treasury Department upon the occurrence of certain events. A failure to comply with the reporting requirements will result in increased monetary penalties.

Information reporting requirements

First, the bill requires the grantor, transferor or executor (i.e., the “responsible party”) to notify the Treasury Department upon the occurrence of certain reportable events. The term “reportable event” means the creation of any foreign trust by a U.S. person, the direct and indirect transfer of any money or property to a foreign trust, including a transfer by reason of death, and the death of a U.S. citizen or resident if any portion of a foreign trust was included in the gross estate of the decedent. A reportable event does not include any transfer of property to a foreign trust in exchange for consideration of at least the fair market value of the property.⁸ Also excluded are transfers to certain pension trusts, nonexempt employees’ trusts described in section 402(b), and charitable trusts. The required return provides information regarding the amount of money or other property transferred to the trust, the identities of the trustee and beneficiaries of the foreign trust, and other items as prescribed by the Secretary of the Treasury.

Second, a U.S. person that is treated as the owner of any portion of a foreign trust is required to ensure that the trust files an annual return to provide full accounting of all the trust activities for the taxable year, the name of the U.S. agent for the trust, and other information as prescribed by the Secretary of the Treasury.⁹ In addition, unless a U.S. person is authorized to accept service of process as the trust’s limited agent with respect to any request by the Treasury Department to examine records or to take testimony, and any summons for such records or testimony, in connection with

⁸For this purpose, consideration other than cash is taken into account at its fair market value and the rules of section 679(a)(3), as modified by the bill, apply (see earlier discussion).

⁹The Committee intends that the Treasury regulations would require the trust to furnish information to U.S. grantors and beneficiaries concerning income reportable by such persons in a manner similar to that used to report the items on schedule K-1 of Form 1041.

the tax treatment of any items related to the trust, the Treasury Secretary is entitled to determine the tax consequences of amounts to be taken into account under the grantor trust rules (secs. 671 through 679). This limited agency relationship does not constitute an agency relationship for any other purpose under Federal or State law. The Committee intends that the Treasury Secretary's exercise of its authority to make such a determination will be subject to judicial review under an arbitrary or capricious standard, which provides a high degree of deference to such determination. For this purpose, rules similar to the rules of sections 6038A(e)(2) and (4) with respect to enforcement of requests for certain records apply.

Third, any U.S. person that receives (directly or indirectly) any distribution from a foreign trust is required to file a return to report the name of the trust, the aggregate amount of the distributions received, and other information that the Secretary of the Treasury may prescribe. In cases where adequate records are not provided to the Secretary of Treasury to determine the proper treatment of any distributions from a foreign trust, the distribution is includable in the gross income of the U.S. distributee and is treated as an accumulation distribution from the middle year of a foreign trust (i.e., computed by taking the number of years that the trust has been in existence divided by 2) for purposes of computing the interest charge applicable to such distribution, unless the foreign trust elects to have a U.S. agent for the limited purpose of accepting service of process (as described above).

Monetary penalties for failure to report

Under the bill, a person that fails to provide the required notice or return in cases involving the transfer of property to a new or existing foreign trust, or a distribution by a foreign trust to a U.S. person, is subject to an initial penalty equal to 35 percent of the gross reportable amount. A failure to provide an annual reporting of trust activities will result in an initial penalty equal to 5 percent of the gross reportable amount.

In cases involving a transfer of property to a foreign trust, the gross reportable amount is the gross value of the property transferred. In cases involving the death of a U.S. citizen or resident whose estate includes any portion of a foreign trust, the gross amount is the greater of: (a) the amount the decedent is treated as owning under the grantor trust rules or (b) the value of the property includable in the gross estate of the decedent. In cases where annual reporting of trust activities is required, the gross reportable amount is the gross value of the portion of the foreign trust's assets treated as owned by the U.S. grantor at the close of the year, and in cases involving a distribution to a U.S. beneficiary of a foreign trust, the gross reportable amount is the amount of the distribution to the beneficiary. An additional \$10,000 penalty is imposed for continued failure for each 30-day period (or fraction thereof) beginning 90 days after the Treasury Department notifies the responsible party of such failure. The same penalties are applicable to a failure to report (as required by present law) certain transfers to other foreign entities. Such penalties are subject to a reasonable cause exception. The Committee intends that the reasonable cause

standard will be satisfied upon the showing of reasonable efforts to comply with the reporting requirements. In no event will the total amount of penalties exceed the gross reportable amount.

Effective date

The reporting requirements and applicable penalties generally apply to reportable events occurring or distributions received after the date of enactment. The annual reporting requirement and penalties applicable to U.S. grantors apply to taxable years of such persons beginning after December 31, 1995.

g. Reporting of foreign gifts

The bill generally requires any U.S. person (other than certain tax-exempt organizations) that receives purported gifts or bequests from foreign sources total more than \$10,000 during the taxable year to report them to the Treasury Department. The threshold for this reporting requirement is indexed for inflation. The definition of a gift to a U.S. person for this purpose excludes amounts that are qualified tuition or medical payments made on behalf of the U.S. person, as defined for gift tax purposes (sec. 2503(e)(2)), and amounts that are distributions to a U.S. beneficiary of a foreign trust if such amounts are properly disclosed under the reporting requirements of the bill. If the U.S. person fails, without reasonable cause, to report foreign gifts as required, the Treasury Secretary is authorized to determine the tax treatment of the unreported gifts. The Committee intends that the Treasury Secretary's exercise of its authority to make such a determination will be subject to judicial review under an arbitrary or capricious standard, which provides a high degree of deference to such determination. In addition, the U.S. person is subject to a penalty equal to 5 percent of the amount of the gift for each month that the failure continues, with the total penalty not to exceed 25 percent of such amount.

Effective date

The provision applies to amounts received after the date of enactment.

III. VOTES OF THE COMMITTEE

In compliance with clause 2(1)(2)(B) of rule XI of the Rules of the House of Representatives, the following statement is made concerning the votes of the Committee in its consideration of the bill:

Motion to report the bill

The bill, H.R. 3286, was ordered favorably reported, as amended, on May 1, 1996, by voice vote, with a quorum present.

Roll call vote on amendment

An amendment by Mr. Rangel, as amended by Mr. Jacobs, to Title II to restore current law language regarding the use of cultural, ethnic or racial considerations in placement of children into foster care or adoptive homes was defeated by a roll call vote of 15 yeas to 22 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X	.....	Mr. Gibbons	X	.....	.....
Mr. Crane		X	.....	Mr. Rangel	X	.....	.....
Mr. Thomas		X	.....	Mr. Stark	X	.....	.....
Mr. Shaw		X	.....	Mr. Jacobs	X	.....	.....
Mrs. Johnson		X	.....	Mr. Ford	X	.....	.....
Mr. Bunning		X	.....	Mr. Matsui	X	.....	.....
Mr. Houghton		X	.....	Mrs. Kennelly	X	.....	.....
Mr. Herger		X	.....	Mr. Coyne	X	.....	.....
Mr. McCreary		X	.....	Mr. Levin	X	.....	.....
Mr. Hancock		X	.....	Mr. Cardin	X	.....	.....
Mr. Camp		X	.....	Mr. McDermott	X	.....	.....
Mr. Ramstad		X	.....	Mr. Kleczka	X	.....	.....
Mr. Zimmer		X	.....	Mr. Lewis .....	.....	.....	.....
Mr. Nussle		X	.....	Mr. Payne	X	.....	.....
Mr. Johnson		X	.....	Mr. Neal	X	.....	.....
Ms. Dunn		X	.....	Mr. McNulty	X	.....	.....
Mr. Collins		X	.....			
Mr. Portman		X	.....			
Mr. Hayes				
Mr. Laughlin		X	.....			
Mr. English		X	.....			
Mr. Ensign		X	.....			
Mr. Christensen		X	.....			

IV. BUDGET EFFECTS OF THE BILL

A. Committee Estimate of Budgetary Effects

In compliance with clause 7(a) of rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effects on the budget of the revenue provisions of the bill, H.R. 3286, as reported.

The revenue provisions of the bill, as amended, are estimated to have the following effects on the budget for fiscal years 1996–2002:

ESTIMATED BUDGET EFFECTS OF THE REVENUE PROVISIONS CONTAINED IN H.R. 3286 AS REPORTED BY THE COMMITTEE ON WAYS AND MEANS, FISCAL YEARS 1996-2002

[In millions of dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	1996-00	1996-02
1. \$5,000 credit for adoption expenses; phase out beginning at \$75,000 AGI; require finalized adoption only for foreign adoptions; special needs adoptions.	tyba 12/31/96	.....	30	305	327	348	354	357	1,010	1,721
2. Remove business exclusion for energy subsidies provided by public utilities	tyba 12/31/96	.....	63	100	104	107	109	111	373	593
3. Modify treatment of foreign trusts	(¹)	.....	143	171	180	188	197	206	734	1,137
Net totals	.....	52	176	34	43	53	48	40	97	9

¹ Various effective dates depending on provisions.

Source: Joint Committee on Taxation.

Note: Details may not add to totals due to rounding.

B. Statement Regarding New Budget Authority and Tax Expenditures

Budget authority

In compliance with subdivision (B) of clause 2(1)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the bill involves no new or increased budget authority.

Tax expenditures

In compliance with subdivision (B) of clause 2(1)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the bill involves a new tax expenditure for the Title I adoption credit and exclusion provisions (sec. 101) and reduced tax expenditures for the Title IV provision relating to exclusion for business energy conservation subsidies (sec. 401). (See the budget table in IV.A., above.)

C. Cost Estimate Prepared by the Congressional Budget Office

In compliance with subdivision (C) of clause 2(1)(3) of rule XI of the Rules of the House of Representatives, requiring a cost estimate prepared by the Congressional Budget Office (CBO), the following statement by CBO is provided.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, May 2, 1996.

Hon. BILL ARCHER,
*Chairman, Committee on Ways and Means,
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office (CBO) has estimated the budgetary effects of H.R. 3286, the Adoption Promotion and Stability Act of 1996, as ordered reported by the Committee on Ways and Means on May 1, 1996. Because H.R. 3286 would affect revenues, H.R. 3286 would be subject to the pay-as-you-go procedures under Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985.

The attached table displays the federal budgetary effects of H.R. 3286. The revenue estimates for Titles I and IV of the bill have been provided by the Joint Committee on Taxation. The total revenue effects of the bill amount to increases of \$52 million in 1996, \$176 million in 1997, and \$9 million over the 1996–2002 period. Titles I and IV contain no intergovernmental mandates, as defined in Public Law 104–4, and would impose no direct costs on state, local, or tribal governments. These titles do, however, contain private sector mandates, as described in the attached private sector mandate statement.

CBO estimates that the provisions of Title II that would remove barriers to interethnic adoptions would have a negligible effect on federal outlays. Although state governments or any other entity in the state that receives any federal funds for adoption or foster care placements could pay penalties for the failure to follow the provisions of Title II, the penalties are sufficiently large that states

would comply with the new provisions, and the penalties collected would be negligible.

Section 4 of the Unfunded Mandates Reform Act of 1995 excludes from the application of that act legislative provisions that establish or enforce statutory rights that prohibit discrimination on the basis of race, color, or national origin. CBO has determined that the provisions in Titles II fit within that exclusion.

The staff contacts are Justin Latus for federal issues and Karen McVey for state, local, and tribal issues.

Sincerely,

JAMES L. BLUM
(For June E. O'Neill, Director).

Attachments.

Estimated budgetary effects of H.R. 3286:

[By fiscal year, in millions of dollars]

	1996	1997	1998	1999	2000	2001	2002
Direct spending							
Title II—Interethnic adoptions:							
Estimated budget authority:	(¹)	(^{1})	(^{1})	(^{1})	(^{1})	(^{1})	(^{1})
Estimated outlays .....	(^{1})	(^{1})	(^{1})	(^{1})	(^{1})	(^{1})	(¹)
Revenues							
Title I—Credit for adoption assistance		-30	-305	-327	-348	-354	-357
Title IV—Revenue Offsets	52	206	271	284	295	306	317
Total:	52	176	-34	-43	-53	-48	-40
Net effect on the deficit	-52	-176	34	43	53	48	40

¹ Indicates less than \$500,000.

Note: Revenue estimates provided by the Joint Committee on Taxation.

Pay-as-you-go considerations:

[By fiscal year, in millions of dollars]

	1996	1997	1998
Change in outlays	0	0	0
Change in revenues	52	176	-34

CONGRESSIONAL BUDGET OFFICE ESTIMATE OF COSTS OF PRIVATE SECTOR MANDATES

1. Bill number: H.R. 3286.
2. Bill title: Adoption Promotion and Stability Act of 1996.
3. Bill status: As ordered reported by the House Committee on Ways and Means on May 1, 1996.
4. Bill purpose: The purpose of the bill is to defray adoption costs and promote the adoption of minority children.
5. Private sector mandates contained in the bill: H.R. 3286 contains mandates as defined in Public Law 104-4 that would affect taxes paid by private sector entities. In particular, the bill would remove the business exclusion for energy subsidies provided by public utilities and modify the treatment of foreign trusts. In addition to these mandates, the bill includes a new credit for adoption expenses that would reduce tax payments.
6. Estimated direct cost to the private sector: The Joint Committee on taxation (JCT) estimates that the direct private sector costs

of the tax increases in H.R. 3286 would be no less than the amounts that appear in the following table.

[Fiscal year in millions of dollars]

	1996	1997	1998	1999	2000
Remove business exclusion for energy subsidies provided by public utilities		63	100	104	107
Modify treatment of foreign trusts	52	143	171	180	188

In addition to these mandates, the bill also provides for a reduction in taxes. At this point, it is unclear to CBO whether under Public law 104-4 this tax reduction should be viewed as an offset to the direct costs of the mandates in the bill. JCT estimates that the savings associated with the tax reduction in H.R. 3286 would be as displayed in the following table.

[Fiscal year in millions of dollars]

	1996	1997	1998	1999	2000
Credit for adoption expenses		-30	-305	-327	-348

7. Appropriations or other Federal financial assistance: None.

8. Previous CBO estimates: None.

9. Estimate prepared by: Daniel Mont (non-tax items) and Rick Kasten (tax items).

10. Estimate approved by: Joseph R. Antos, Assistant Director for Health and Human Resources.

V. OTHER MATTERS TO BE DISCUSSED UNDER THE RULES OF THE HOUSE

A. Committee Oversight Findings and Recommendations

With respect to subdivision (A) of clause 2(1)(3) of rule XI of the Rules of the House of Representatives (relating to oversight findings), the Committee advises that it was the result of the Committee's oversight activities concerning the encouragement of adoptions of children and the costs of adoptions to families, barriers to interethnic adoptions, and needed revenue offsets (repealing the exclusion for business energy conservation subsidies provided by utilities and modification of the foreign trust tax rules) that the Committee concluded that it is appropriate and timely to enact the provisions contained in the bill as amended.

B. Summary of Findings and Recommendations of the Committee on Government Reform and Oversight

With respect to subdivision (D) of clause 2(1)(3) of Rule XI of the Rules of the House of Representatives, the Committee advises that no oversight findings or recommendations have been submitted to this Committee by the Committee on Government Reform and Oversight with respect to the provisions contained in the bill.

C. Inflationary Impact Statement

In compliance with clause 2(1)(4) of rule XI of the Rules of the House of Representatives, the Committee states that the provisions

of the bill are not expected to have an overall inflationary impact on prices and costs in the national economy.

D. Information Relating to Unfunded Mandates

This information is provided in accordance with section 423 of the Unfunded Mandates Act of 1995 (P.L. 104-4).

The Committee has determined that two of the revenue provisions of the bill contain Federal mandates on the private sector: (1) the provision to remove the business exclusion for energy subsidies provided by public utilities and (2) the provision to modify the treatment of foreign trusts. The first provision repeals an exclusion from gross income for energy subsidies provided to a business by a public utility. The second provision changes the tax treatment applicable to trusts and modifies the information reporting requirements and penalties applicable to foreign trusts. These two provisions will increase the Federal tax liabilities of certain taxpayers and, in the case of the foreign trust provisions, will also impose costs related to the new recordkeeping and reporting requirements imposed by the bill.

The cost required to comply with each mandate generally is no greater than the revenue estimate for the provision. Benefits from the provisions include improved administration of the Federal income tax laws and a more accurate measurement of gross income for Federal income tax purposes. The Committee believes the benefits of the bill are greater than the costs required to comply with the Federal private sector mandates contained in the bill.

The provision relating to the business energy exclusion results in a better measurement of gross income for Federal income tax purposes. A business would be permitted to depreciate any property received by a public utility that previously had been excluded from income. Therefore, relative to the revenue estimate, the cost of the Federal private sector mandate is reduced to the extent of future depreciation deductions permitted.

The provisions modifying the treatment of foreign trusts contain Federal private sector mandates to the extent the provisions impose new reporting requirements and recharacterize the income of such trusts to ensure that U.S. Federal income tax is paid. In general, these rules are designed to reflect changes in the uses of foreign trusts and to limit the avoidance of U.S. taxes through the use of such trusts.

The revenue-raising provisions of the bill are used to offset the cost of providing a tax credit to individuals who adopt a child. This tax credit furthers the social policy goal of ensuring that families who desire to adopt a child have the financial resources to do so. The revenue-raising provisions are critical to achieving this goal.

The revenue provisions of the bill do not contain any intergovernmental mandates.

The revenue provisions of the bill affect activities that are only engaged in by the private sector and, thus, do not affect the competitive balance between State, local, or tribal governments and the private sector.

E. Applicability of House Rule XXI5(c)

Rule XXI5(c) of the Rules of the House of Representatives provides that “No bill or joint resolution, amendment, or conference report carrying a Federal income tax rate increase shall be considered as passed or agreed to unless so determined by a vote of not less than three-fifths of the Members voting.” The Committee has carefully reviewed the provisions of the bill to determine whether any of these provisions constitute a Federal income tax rate increase within the meaning of the House rules. It is the opinion of the Committee that there is no provision in the bill that constitutes a Federal income tax rate increase within the meaning of House rule XXI5(c) or (d).

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman).

INTERNAL REVENUE CODE OF 1986

Subtitle A—Income Taxes

* * * * *

CHAPTER 1—NORMAL TAXES AND SURTAXES

* * * * *

Subchapter A—Determination of Tax Liability

* * * * *

PART IV—CREDITS AGAINST TAX

* * * * *

Subpart A—Nonrefundable Personal Credits

Sec. 21. Expenses for household and dependent care services necessary for gainful employment.

* * * * *

Sec. 23. *Adoption expenses.*

* * * * *

SEC. 23. ADOPTION EXPENSES.

(a) *ALLOWANCE OF CREDIT.*—*In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year the amount of the qualified adoption expenses paid or incurred by the taxpayer during such taxable year.*

(b) *LIMITATIONS.*—

(1) *DOLLAR LIMITATION.*—The aggregate amount of qualified adoption expenses which may be taken into account under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed \$5,000.

(2) *INCOME LIMITATION.*—The amount allowable as a credit under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so allowable (determined without regard to this paragraph but with regard to paragraph (1)) as—

(A) the amount (if any) by which the taxpayer's adjusted gross income (determined without regard to sections 911, 931, and 933) exceeds \$75,000, bears to

(B) \$40,000.

(3) *DENIAL OF DOUBLE BENEFIT.*—

(A) *IN GENERAL.*—No credit shall be allowed under subsection (a) for any expense for which a deduction or credit is allowable under any other provision of this chapter.

(B) *GRANTS.*—No credit shall be allowed under subsection (a) for any expense to the extent that funds for such expense are received under any Federal, State, or local program. The preceding sentence shall not apply to expenses for the adoption of a child with special needs.

(C) *REIMBURSEMENT.*—No credit shall be allowed under subsection (a) for any expense to the extent that such expense is reimbursed and the reimbursement is excluded from gross income under section 137.

(c) *CARRYFORWARDS OF UNUSED CREDIT.*—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of the credits allowable under this subpart (other than this section), such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such taxable year. No credit may be carried forward under this subsection to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For purposes of the preceding sentence, credits shall be treated as used on a first-in first-out basis.

(d) *DEFINITIONS.*—For purposes of this section—

(1) *QUALIFIED ADOPTION EXPENSES.*—The term 'qualified adoption expenses' means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses—

(A) which are directly related to, and the principal purpose of which is for, the legal adoption of an eligible child by the taxpayer, and

(B) which are not incurred in violation of State or Federal law or in carrying out any surrogate parenting arrangement.

(2) *EXPENSES FOR ADOPTION OF SPOUSE'S CHILD NOT ELIGIBLE.*—The term 'qualified adoption expenses' shall not include any expenses in connection with the adoption by an individual of a child who is the child of such individual's spouse.

(3) *ELIGIBLE CHILD.*—The term 'eligible child' means any individual—

(A) who has not attained age 18 as of the time of the adoption, or

(B) who is physically or mentally incapable of caring for himself.

(4) CHILD WITH SPECIAL NEEDS.—The term ‘child with special needs’ means any child if—

(A) a State has determined that the child cannot or should not be returned to the home of his parents, and

(B) such State has determined that there exists with respect to the child a specific factor or condition (such as his ethnic background, age, or membership in a minority or sibling group, or the presence of factors such as medical conditions or physical, mental, or emotional handicaps) because of which it is reasonable to conclude that such child cannot be placed with adoptive parents without providing adoption assistance.

(e) SPECIAL RULES FOR FOREIGN ADOPTIONS.—In the case of a foreign adoption—

(1) subsection (a) shall not apply to any qualified adoption expense with respect to such adoption unless such adoption becomes final, and

(2) any such expense which is paid or incurred before the taxable year in which such adoption becomes final shall be taken into account under this section as if such expense were paid or incurred during such year.

(f) MARRIED COUPLES MUST FILE JOINT RETURNS.—Rules similar to the rules of paragraphs (2), (3), and (4) of section 21(e) shall apply for purposes of this section.

(g) BASIS ADJUSTMENTS.—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out this section and section 137, including regulations which treat unmarried individuals who pay or incur qualified adoption expenses with respect to the same child as 1 taxpayer for purposes of applying the dollar limitation in subsection (b)(1) of this section and in section 137(b)(1).

* * * * *

Subchapter B—Computation of Taxable Income

* * * * *

PART II—ITEMS SPECIFICALLY INCLUDED IN GROSS INCOME

* * * * *

SEC. 86. SOCIAL SECURITY AND TIER 1 RAILROAD RETIREMENT BENEFITS.

(a) * * *

(b) TAXPAYERS TO WHOM SUBSECTION (a) APPLIES.—

(1) * * *

(2) MODIFIED ADJUSTED GROSS INCOME.—For purposes of this subsection, the term “modified adjusted gross income” means adusted gross income—

(A) determined without regard to this section and sections 135, 137, 911, 931, and 933, and

(B) increased by the amount of interest received or accrued by the taxpayer during the taxable year which is exempt from tax.

* * * * *

PART III—ITEMS SPECIFICALLY EXCLUDED FROM GROSS INCOME

Sec. 101. Certain death benefits.

* * * * *

[Sec. 137. Cross reference to other Acts.]
Sec. 137. Adoption assistance programs.
Sec. 138. Cross reference to other Acts.

* * * * *

SEC. 135. INCOME FROM UNITED STATES SAVINGS BONDS USED TO PAY HIGHER EDUCATION TUITION AND FEES

(a) * * *

* * * * *

(c) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * *

(4) MODIFIED ADJUSTED GROSS INCOME.—The term “modified adjusted gross income” means the adjusted gross income of the taxpayer for the taxable year determined—

(A) without regard to this section and sections 137, 911, 931, and 933, and

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

* * * * *

SEC. 136. ENERGY CONSERVATION SUBSIDIES PROVIDED BY PUBLIC UTILITIES.

[(a) EXCLUSION.—

[(1) IN GENERAL.—Gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure.

[(2) LIMITATION ON EXCLUSION FOR NONRESIDENTIAL PROPERTY.—

[(A) IN GENERAL.—In the case of any subsidy provided with respect to any energy conservation measure referred to in subsection (c)(1)(B), only the applicable percentage of such subsidy shall be excluded from gross income under paragraph (1).

[(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the term “applicable percentage” means—

[(i) 40 percent in the case of subsidies provided during 1995,

[(ii) 50 percent in the case of subsidies provided during 1996, and

[(iii) 65 percent in the case of subsidies provided after 1996.]

(a) *EXCLUSION.*—*Gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure.*

* * * * *

(c) **ENERGY CONSERVATION MEASURE.**—

(1) **IN GENERAL.**—For purposes of this section, the term “energy conservation measure” means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of [energy demand—

[(A) with respect to a dwelling unit, and

[(B) on or after January 1, 1995, with respect to property other than dwelling units.

The purchase and installation of specially defined energy property shall be treated as an energy conservation measure described in subparagraph (B).] *energy demand with respect to a dwelling unit.*

(2) **OTHER DEFINITIONS [AND SPECIAL RULES].**—For purposes of this subsection—

[(A) **SPECIALLY DEFINED ENERGY PROPERTY.**—The term “specially defined energy property” means—

[(i) a recuperator,

[(ii) a heat wheel,

[(iii) a regenerator,

[(iv) a heat exchanger,

[(v) a waste heat boiler,

[(vi) a heat pipe,

[(vii) an automatic energy control system,

[(viii) a turbulator,

(ix) a preheater,

[(x) a combustible gas recovery system,

[(xi) an economizer,

[(xii) modifications to alumina electrolytic cells,

[(xiii) modifications to chlor-alkali electrolytic cells,

or

[(xiv) any other property of a kind specified by the Secretary by regulations, the principal purpose of which is reducing the amount of energy consumed in any existing industrial or commercial process and which is installed in connection with an existing industrial or commercial facility.]

[(B) **(A) DWELLING UNIT.**—The term “dwelling unit” has the meaning given such term by section 280A(f)(1).

[(C) **(B) PUBLIC UTILITY.**—The term “public utility” means a person engaged in the sale of electricity or natural gas to residential, commercial, or industrial customers for use by such customers. For purposes of the preceding sentence, the term ‘person’ includes the Federal Government, a State or local government or any political subdivi-

sion thereof, or any instrumentality of any of the foregoing.

* * * * *

SEC. 137. ADOPTION ASSISTANCE PROGRAMS.

(a) *IN GENERAL.*—Gross income of an employee does not include amounts paid or expenses incurred by the employer for qualified adoption expenses in connection with the adoption of a child by an employee if such amounts are furnished pursuant to an adoption assistance program.

(b) *LIMITATIONS.*—

(1) *DOLLAR LIMITATION.*—The aggregate amount excludable from gross income under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed \$5,000.

(2) *INCOME LIMITATION.*—The amount excludable from gross income under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so excludable (determined without regard to this paragraph but with regard to paragraph (1)) as—

(A) the amount (if any) by which the taxpayer's adjusted gross income exceeds \$75,000, bears to

(B) \$40,000.

(3) *DETERMINATION OF ADJUSTED GROSS INCOME.*—For purposes of paragraph (2), adjusted gross income shall be determined—

(A) without regard to this section and sections 911, 931, and 933, and

(B) after the application of sections 86, 135, 219, and 469.

(c) *ADOPTION ASSISTANCE PROGRAM.*—For purposes of this section, an adoption assistance program is a plan of an employer—

(1) under which the employer provides employees with adoption assistance, and

(2) which meets requirements similar to the requirements of paragraphs (2), (3), and (5) of section 127(b).

An adoption reimbursement program operated under section 1052 of title 10, United States Code (relating to armed forces) or section 514 of title 14, United States Code (relating to members of the Coast Guard) shall be treated as an adoption assistance program for purposes of this section.

(d) *QUALIFIED ADOPTION EXPENSES.*—For purposes of this section, the term 'qualified adoption expenses' has the meaning given such term by section 23(d).

(e) *CERTAIN RULES TO APPLY.*—Rules similar to the rules of subsections (e) and (g) of section 23 shall apply for purposes of this section.

SEC. [137.] 138. CROSS REFERENCE TO OTHER ACTS.

(a) * * *

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PART VII—ADDITIONAL ITEMIZED DEDUCTIONS FOR INDIVIDUALS

* * * * *

SEC. 219. RETIREMENT SAVINGS.

(a) * * *

* * * * *

(g) **LIMITATION ON DEDUCTION FOR ACTIVE PARTICIPANTS IN CERTAIN PENSION PLANS.—**

(1) * * *

* * * * *

(3) **ADJUSTED GROSS INCOME; APPLICABLE DOLLAR AMOUNT.—**
For purposes of this subsection—

(A) **ADJUSTED GROSS INCOME.—**Adjusted gross income of any taxpayer shall be determined—

(i) after application of sections 86 and 469, and

(ii) without regard to sections 135, 137, and 911 or the deduction allowable under this section.

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Subchapter E—Accounting Periods and Methods of Accounting

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PART II—METHODS OF ACCOUNTING

* * * * *

Subpart C—Taxable Year for Which Deductions Taken

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SEC. 469. PASSIVE ACTIVITY LOSSES AND CREDITS LIMITED.

(a) * * *

* * * * *

(i) **\$25,000 OFFSET FOR RENTAL REAL ESTATE ACTIVITIES.—**

(1) * * *

* * * * *

(3) **PHASE-OUT OF EXEMPTION.—**

(A) * * *

* * * * *

(E) **ADJUSTED GROSS INCOME.—**For purposes of this paragraph, adjusted gross income shall be determined without regard to—

(i) any amount includible in gross income under section 86,

[(ii) the amount excludable from gross income under section 135,]

(ii) the amounts excludable from gross income under sections 135 and 137,

* * * * *

Subchapter J—Estates, Trusts, Beneficiaries, and Dependents

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PART I—ESTATES, TRUSTS, AND BENEFICIARIES

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Subpart A—General Rules for Taxation of Estates and Trusts

* * * * *

SEC. 643. DEFINITIONS APPLICABLE TO SUBPARTS A, B, C, AND D

(a) **DISTRIBUTABLE NET INCOME.**—For purposes of this part, the term “distributable net income” means, with respect to any taxable year, the taxable income of the estate or trust computed with the following modifications—

(1) * * *

* * * * *

(7) **ABUSIVE TRANSACTIONS.**—*The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent avoidance of such purposes.*

* * * * *

(h) **DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.**—*For purposes of this part, any amount paid to a United States person which is derived directly or indirectly from a foreign trust of which the payor is not the grantor shall be deemed in the year of payment to have been directly paid by the foreign trust to such United States person.*

(i) **LOANS FROM FOREIGN TRUSTS.**—*For purposes of subparts B, C, and D—*

(1) **GENERAL RULE.**—*Except as provided in regulations, if a foreign trust makes a loan of cash or marketable securities directly or indirectly to—*

(A) *any grantor or beneficiary of such trust who is a United States person, or*

(B) *any United States person not described in subparagraph (A) who is related to such grantor or beneficiary, the amount of such loan shall be treated as a distribution by such trust to such grantor or beneficiary (as the case may be).*

(2) **DEFINITIONS AND SPECIAL RULES.**—*For purposes of this subsection—*

(A) **CASH.**—*The term “cash” includes foreign currencies and cash equivalents.*

(B) **RELATED PERSON.**—

(i) **IN GENERAL.**—*A person is related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the preceding sentence, section 267(c)(4) shall be applied as if the family of an individual includes the spouses of the members of the family.*

(ii) ALLOCATION.—If any person described in paragraph (1)(B) is related to more than one person, the grantor or beneficiary to whom the treatment under this subsection applies shall be determined under regulations prescribed by the Secretary.

(C) EXCLUSION OF TAX-EXEMPTS.—The term “United States person” does not include any entity exempt from tax under this chapter.

(D) TRUST NOT TREATED AS SIMPLE TRUST.—Any trust which is treated under this subsection as making a distribution shall be treated as not described in section 651.

(3) SUBSEQUENT TRANSACTIONS REGARDING LOAN PRINCIPAL.—If any loan is taken into account under paragraph (1), any subsequent transaction between the trust and the original borrower regarding the principal of the loan (by way of complete or partial repayment, satisfaction, cancellation, discharge, or otherwise) shall be disregarded for purposes of this title.

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Subpart D—Treatment of Excess Distribution by Trusts

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SEC. 665. DEFINITIONS APPLICABLE TO SUBPART D

(a) * * *

* * * * *

[(c) SPECIAL RULE APPLICABLE TO DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS.—For purposes of this subpart, any amount paid to a United States person which is from a payor who is not a United States person and which is derived directly or indirectly from a foreign trust created by a United States person shall be deemed in the year of payment to have been directly paid by the foreign trust.]

(d) TAXES IMPOSED ON THE TRUST.—For purposes of this subpart—

(1) * * *

(2) FOREIGN TRUSTS.—In the case of any foreign trust, the term “taxes imposed on the trust” includes the amount, reduced as provided in the last sentence of paragraph (1), of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on such foreign trust which, as determined under paragraph (1), are so properly allocable. Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the term “taxes imposed on the trust” includes the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust gross income.

* * * * *

SEC. 668. INTEREST CHARGE ON ACCUMULATION DISTRIBUTIONS FROM FOREIGN TRUSTS.

[(a) GENERAL RULE.—For purposes of the tax determined under section 667(a), the interest charge is an amount equal to 6 percent of the partial tax computed under section 667(b) multiplied by a fraction—

[(1) the numerator of which is the sum of the number of taxable years between each taxable year to which the distribution is allocated under section 666(a) and the taxable year of the distribution (counting in each case the taxable year to which the distribution is allocated but not counting the taxable year of the distribution), and

[(2) the denominator of which is the number of taxable years to which the distribution is allocated under section 666(a).]

(a) GENERAL RULE.—For purposes of the tax determined under section 667(a)—

(1) INTEREST DETERMINED USING UNDERPAYMENT RATES.—*The interest charge determined under this section with respect to any distribution is the amount of interest which would be determined on the partial tax computed under section 667(b) for the period described in paragraph (2) using the rates and the method under section 6621 applicable to underpayments of tax.*

(2) PERIOD.—*For purposes of paragraph (1), the period described in this paragraph is the period which begins on the date which is the applicable number of years before the date of the distribution and which ends on the date of the distribution.*

(3) APPLICABLE NUMBER OF YEARS.—*For purposes of paragraph (2)—*

(A) IN GENERAL.—*The applicable number of years with respect to a distribution is the number determined by dividing—*

(i) *the sum of the products described in subparagraph (B) with respect to each undistributed income year, by*

(ii) *the aggregate undistributed net income.*

The quotient determined under the preceding sentence shall be rounded under procedures prescribed by the Secretary.

(B) PRODUCT DESCRIBED.—*For purposes of subparagraph (A), the product described in this subparagraph with respect to any undistributed income year is the product of—*

(i) *the undistributed net income for such year, and*

(ii) *the sum of the number of taxable years between such year and the taxable year of the distribution (counting in each case the undistributed income year but not counting the taxable year of the distribution).*

(4) UNDISTRIBUTED INCOME YEAR.—*For purposes of this subsection, the term “undistributed income year” means any prior taxable year of the trust for which there is undistributed net income, other than a taxable year during all of which the beneficiary receiving the distribution was not a citizen or resident of the United States.*

(5) DETERMINATION OF UNDISTRIBUTED NET INCOME.—*Notwithstanding section 666, for purposes of this subsection, an accumulation distribution from the trust shall be treated as re-*

ducing proportionately the undistributed net income for undistributed income years.

(6) PERIODS BEFORE 1996.—Interest for the portion of the period described in paragraph (2) which occurs before January 1, 1996, shall be determined—

(A) by using an interest rate of 6 percent, and

(B) without compounding until January 1, 1996.

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Subpart E—Grantor and Others Treated as Substantial Owners

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SEC. 672. DEFINITIONS AND RULES.

(a) * * *

* * * * *

(c) RELATED OR SUBORDINATE PARTY.—For purposes of this subpart, the term “related or subordinate party” means any non-adverse party who is—

(1) the grantor’s spouse if living with the grantor;

(2) any one of the following: The grantor’s father, mother, issue, brother or sister; an employee of the grantor; a corporation or any employee of a corporation in which the stock holdings of the grantor and the trust are significant from the viewpoint of voting control; a subordinate employee of a corporation in which the grantor is an executive.

For purposes of *subsection (f) and sections 674 and 675*, a related or subordinate party shall be presumed to be subservient to the grantor in respect of the exercise or nonexercise of the powers conferred on him unless such party is shown not to be subservient by a preponderance of the evidence.

* * * * *

[(f) SPECIAL RULE WHERE GRANTOR IS FOREIGN PERSON.—

[(1) IN GENERAL.—If—

[(A) but for this subsection, a foreign person would be treated as the owner of any portion of a trust, and

[(B) such trust has a beneficiary who is a United States person,

such beneficiary shall be treated as the grantor of such portion to the extent such beneficiary has made transfers of property by gift (directly or indirectly) to such foreign person. For purposes of the preceding sentence, any gift shall not be taken into account to the extent such gift would be excluded from taxable gifts under section 2503(b).

[(2) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection.]

(f) SUBPART NOT TO RESULT IN FOREIGN OWNERSHIP.—

(1) IN GENERAL.—*Notwithstanding any other provision of this subpart, this subpart shall apply only to the extent such application results in an amount being currently taken into account (directly or through 1 or more entities) under this chapter in*

computing the income of a citizen or resident of the United States or a domestic corporation.

(2) *EXCEPTIONS.*—

(A) *CERTAIN REVOCABLE AND IRREVOCABLE TRUSTS.*—

Paragraph (1) shall not apply to any trust if—

(i) the power to revest absolutely in the grantor title to the trust property is exercisable solely by the grantor without the approval or consent of any other person or with the consent of a related or subordinate party who is subservient to the grantor, or

(ii) the only amounts distributable from such trust (whether income or corpus) during the lifetime of the grantor are amounts distributable to the grantor or the spouse of the grantor.

(B) *COMPENSATORY TRUSTS.*—Except as provided in regulations, paragraph (1) shall not apply to any portion of a trust distributions from which are taxable as compensation for services rendered.

(3) *SPECIAL RULES.*—Except as otherwise provided in regulations prescribed by the Secretary—

(A) a controlled foreign corporation (as defined in section 957) shall be treated as a domestic corporation for purposes of paragraph (1), and

(B) paragraph (1) shall not apply for purposes of applying section 1296.

(4) *RECHARACTERIZATION OF PURPORTED GIFTS.*—In the case of any transfer directly or indirectly from a partnership or foreign corporation which the transferee treats as a gift or bequest, the Secretary may recharacterize such transfer in such circumstances as the Secretary determines to be appropriate to prevent the avoidance of the purposes of this subsection.

(5) *SPECIAL RULE WHERE GRANTOR IS FOREIGN PERSON.*—

If—(A) but for this subsection, a foreign person would be treated as the owner of any portion of a trust, and

(B) such trust has a beneficiary who is a United States person,

such beneficiary shall be treated as the grantor of such portion to the extent such beneficiary has made transfers of property by gift (directly or indirectly) to such foreign person. For purposes of the preceding sentence, any gift shall not be taken into account to the extent such gift would be excluded from taxable gifts under section 2503(b).

(6) *REGULATIONS.*—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including regulations providing that paragraph (1) shall not apply in appropriate cases.

* * * * *

SEC. 679. FOREIGN TRUSTS HAVING ONE OR MORE UNITED STATES BENEFICIARIES.

(a) *TRANSFEROR TREATED AS OWNER.*—

(1) *IN GENERAL.*— A United States person who directly or indirectly transfers property to a foreign trust (other than a trust described in [section 404(a)(4) or section 404A]

6048(a)(3)(B)(ii)) shall be treated as the owner for his taxable year of the portion of such trust attributable to such property if for such year there is a United States beneficiary of any portion of such trust.

(2) EXCEPTIONS.— Paragraph (1) shall not apply—

(A) TRANSFERS BY REASON OF DEATH.—To any transfer by reason of the death of the transferor.

[(B) TRANSFERS WHERE GAIN IS RECOGNIZED TO TRANSFEROR.—To any sale or exchange of the property at its fair market value in a transaction in which all of the gain to the transferor is realized at the time of the transfer and is recognized either at such time or is returned as provided in section 453.]

(B) TRANSFERS AT FAIR MARKET VALUE.—To any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value.

* * * * *

(3) CERTAIN OBLIGATIONS NOT TAKEN INTO ACCOUNT UNDER FAIR MARKET VALUE EXCEPTION.—

(A) IN GENERAL.—In determining whether paragraph (2)(B) applies to any transfer by a person described in clause (ii) or (iii) of subparagraph (C), there shall not be taken into account—

(i) except as provided in regulations, any obligation of a person described in subparagraph (C), and

(ii) to the extent provided in regulations, any obligation which is guaranteed by a person described in subparagraph (C).

(B) TREATMENT OF PRINCIPAL PAYMENTS ON OBLIGATION.—Principal payments by the trust on any obligation referred to in subparagraph (A) shall be taken into account on and after the date of the payment in determining the portion of the trust attributable to the property transferred.

(C) PERSONS DESCRIBED.—The persons described in this subparagraph are—

(i) the trust,

(ii) any grantor or beneficiary of the trust, and

(iii) any person who is related (within the meaning of section 643(i)(2)(B)) to any grantor or beneficiary of the trust.

(4) SPECIAL RULES APPLICABLE TO FOREIGN GRANTOR WHO LATER BECOMES A UNITED STATES PERSON.—

(A) IN GENERAL.—If a nonresident alien individual has a residency starting date within 5 years after directly or indirectly transferring property to a foreign trust, this section and section 6048 shall be applied as if such individual transferred to such trust on the residency starting date an amount equal to the portion of such trust attributable to the property transferred by such individual to such trust in such transfer.

(B) TREATMENT OF UNDISTRIBUTED INCOME.—For purposes of this section, undistributed net income for periods

before such individual's residency starting date shall be taken into account in determining the portion of the trust which is attributable to property transferred by such individual to such trust but shall not otherwise be taken into account.

(C) RESIDENCY STARTING DATE.—For purposes of this paragraph, an individual's residency starting date is the residency starting date determined under section 7701(b)(2)(A).

(5) OUTBOUND TRUST MIGRATIONS.—If—

(A) an individual who is a citizen or resident of the United States transferred property to a trust which was not a foreign trust, and

(B) such trust becomes a foreign trust while such individual is alive,

then this section and section 6048 shall be applied as if such individual transferred to such trust on the date such trust becomes a foreign trust an amount equal to the portion of such trust attributable to the property previously transferred by such individual to such trust. A rule similar to the rule of paragraph (4)(B) shall apply for purposes of this paragraph.

* * * * *

(c) TRUSTS TREATED AS HAVING A UNITED STATES BENEFICIARY.—

*(1) * * **

(2) ATTRIBUTION OF OWNERSHIP.—For purposes of paragraph (1), an amount shall be treated as paid or accumulated to or for the benefit of a United States person if such amount is paid to or accumulated for a foreign corporation, foreign partnership, or foreign trust or estate, and—

[(A) in the case of a foreign corporation, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation is owned (within the meaning of section 958(a)) or is considered to be owned (within the meaning of section 958(b)) by United States shareholders (as defined in section 951(b)),]

(A) in the case of a foreign corporation, such corporation is a controlled foreign corporation (as defined in section 957(a)),

(B) in the case of a foreign partnership, a United States person is a partner of such partnership, or

(C) in the case of a foreign trust or estate, such trust or estate has a United States beneficiary (within the meaning of paragraph (1)).

(3) CERTAIN UNITED STATES BENEFICIARIES DISREGARDED.—A beneficiary shall not be treated as a United States person in applying this section with respect to any transfer of property to foreign trust if such beneficiary first became a United States person more than 5 years after the date of such transfer.

(d) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

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**Subchapter N—Tax Based on Income From
Sources Within or Without the United States**

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**PART III—INCOME FROM SOURCES WITHOUT THE
UNITED STATES**

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Subpart A—Foreign Tax Credit

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**SEC. 901. TAXES OF FOREIGN COUNTRIES AND OF POSSESSIONS OF
UNITED STATES.**

(a) * * *

* * * * *

(b) AMOUNT ALLOWED.—Subject to the limitation of section 904, the following amounts shall be allowed as the credit under subsection (a):

(1) * * *

* * * * *

(5) PARTNERSHIPS AND ESTATES.—In the case of any individual described in paragraph (1), (2), (3), or (4), who is a member of a partnership or a beneficiary of an estate or trust, the amount of his proportionate share of the taxes (described in such paragraph) of the partnership or the estate or trust paid or accrued during the taxable year to a foreign country or to any possession of the United States, as the case may be. *Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.*

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**Subchapter O—Gain or Loss on Disposition of
Property**

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PART II—BASIS RULES OF GENERAL APPLICATION

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1016. ADJUSTMENTS TO BASIS.

(a) GENERAL RULE.—Proper adjustment in respect of the property shall in all cases be made—

(1) * * *

* * * * *

(24) to the extent provided in section 179A(e)(6)(A), [and]

(25) to the extent provided in section 30(d)(1)[.]; and
(26) to the extent provided in sections 23(g) and 137(e).

* * * * *

**CHAPTER 5—TAX ON TRANSFERS TO AVOID
INCOME TAX**

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SEC. 1491. IMPOSITION OF TAX.

There is hereby imposed on the transfer of property by a citizen or resident of the United States, or by a domestic corporation or partnership, or by an estate or trust which is not a foreign estate or trust, to a foreign corporation as paid-in surplus or as a contribution to capital, or to a foreign estate or trust, or to a foreign partnership, an excise tax equal to 35 percent of the excess of—

- (1) the fair market value of the property so transferred, over
- (2) the sum of—
 - (A) the adjusted basis (for determining gain) of such property in the hands of the transferor, plus
 - (B) the amount of the gain recognized to the transferor at the time of the transfer.

If a trust which is not a foreign trust becomes a foreign trust, such trust shall be treated for purposes of this section as having transferred, immediately before becoming a foreign trust, all of its assets to a foreign trust.

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SEC. 1494. PAYMENT AND COLLECTION.

(a) * * *

* * * * *

(c) *PENALTY.—In the case of any failure to file a return required by the Secretary with respect to any transfer described in section 1491, the person required to file such return shall be liable for the penalties provided in section 6677 in the same manner as if such failure were a failure to file a notice under section 6048(a).*

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Subtitle F—Procedure and Administration

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CHAPTER 61—INFORMATION AND RETURNS

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Subchapter A—Returns and Records

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PART III—INFORMATION AND RETURNS

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Subpart A—Information Concerning Persons Subject to Special Provisions

Sec. 6031. Return of partnership income.

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Sec. 6039E. Information concerning resident status.

Sec. 6039F. Notice of large gifts received from foreign persons.

* * * * *

SEC. 6039F. NOTICE OF LARGE GIFTS RECEIVED FROM FOREIGN PERSONS.

(a) *IN GENERAL.*—If the value of the aggregate foreign gifts received by a United States person (other than an organization described in section 501(c) and exempt from tax under section 501(a)) during any taxable year exceeds \$10,000, such United States person shall furnish (at such time and in such manner as the Secretary shall prescribe) such information as the Secretary may prescribe regarding each foreign gift received during such year.

(b) *FOREIGN GIFT.*—For purposes of this section, the term “foreign gift” means any amount received from a person other than a United States person which the recipient treats as a gift or bequest. Such term shall not include any qualified transfer (within the meaning of section 2503(e)(2)) or any distribution properly disclosed in a return under section 6048(c).

(c) *PENALTY FOR FAILURE TO FILE INFORMATION.*—

(1) *IN GENERAL.*—If a United States person fails to furnish the information required by subsection (a) with respect to any foreign gift within the time prescribed therefor (including extensions)—

(A) the tax consequences of the receipt of such gift shall be determined by the Secretary, and

(B) such United States person shall pay (upon notice and demand by the Secretary and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month for which the failure continues (not to exceed 25 percent of such amount in the aggregate).

(2) *REASONABLE CAUSE EXCEPTION.*—Paragraph (1) shall not apply to any failure to report a foreign gift if the United States person shows that the failure is due to reasonable cause and not due to willful neglect.

(d) *COST-OF-LIVING ADJUSTMENT.*—In the case of any taxable year beginning after December 31, 1996, the \$10,000 amount under subsection (a) shall be increased by an amount equal to the product of such amount and the cost-of-living adjustment for such taxable year under section 1(f)(3), except that subparagraph (B) thereof shall be applied by substituting “1995” for “1992”.

(e) *REGULATIONS.*—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

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**Subpart B—Information Concerning Transactions with
Other Persons**

Sec. 6041. Information at source.

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【Sec. 6048. Returns as to certain foreign trusts.】
Sec. 6048. Information with respect to certain foreign trusts.

* * * * *

【SEC. 6048. RETURNS AS TO CERTAIN FOREIGN TRUSTS.

【(a) GENERAL RULE.—On or before the 90th day (or on or before such later day as the Secretary may by regulations prescribe) after—

 【(1) the creation of any foreign trust by a United States person, or

 【(2) the transfer of any money or property to a foreign trust by a United States person,

the grantor in the case of an inter vivos trust, the fiduciary of an estate in the case of a testamentary trust, or the transferor, as the case may be, shall make a return in compliance with the provisions of subsection (b).

【(b) FORM AND CONTENTS OF RETURNS.—The returns required by subsection (a) shall be in such form and shall set forth, in respect of the foreign trust, such information as the Secretary prescribes by regulation as necessary for carrying out the provisions of the income tax laws.

【(c) ANNUAL RETURNS FOR FOREIGN TRUSTS HAVING ONE OR MORE UNITED STATES BENEFICIARIES.—Each taxpayer subject to tax under section 679 (relating to foreign trusts having one or more United States beneficiaries) for his taxable year with respect to any trust shall make a return with respect to such trust for such year at such time and in such manner, and setting forth such information, as the Secretary may by regulations prescribe.

【(d) CROSS REFERENCE.—

【For provisions relating to penalties for violation of this section, see sections 6677 and 7203.】

SEC. 6048. INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

(a) NOTICE OF CERTAIN EVENTS.—

(1) GENERAL RULE.—On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).

(2) CONTENTS OF NOTICE.—The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—

(A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and

(B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.

(3) REPORTABLE EVENT.—For purposes of this subsection—

(A) IN GENERAL.—The term “reportable event” means—

(i) the creation of any foreign trust by a United States person,

(ii) the transfer of any money or property (directly or indirectly) to a foreign trust by a United States person, including a transfer by reason of death, and

(iii) the death of a citizen or resident of the United States if—

(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

(II) any portion of a foreign trust was included in the gross estate of the decedent.

(B) EXCEPTIONS.—

(i) **FAIR MARKET VALUE SALES.**—Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

(ii) **DEFERRED COMPENSATION AND CHARITABLE TRUSTS.**—Subparagraph (A) shall not apply with respect to a trust which is—

(I) described in section 402(b), 404(a)(4), or 404A, or

(II) determined by the Secretary to be described in section 501(c)(3).

(4) RESPONSIBLE PARTY.—For purposes of this subsection, the term “responsible party” means—

(A) the grantor in the case of the creation of an inter vivos trust,

(B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and

(C) the executor of the decedent’s estate in any other case.

(b) UNITED STATES GRANTOR OF FOREIGN TRUST.—

(1) IN GENERAL.—If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall be responsible to ensure that—

(A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and

(B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.

(2) TRUSTS NOT HAVING UNITED STATES AGENT.—

(A) IN GENERAL.—If the rules of this paragraph apply to any foreign trust, the determination of amounts required to be taken into account with respect to such trust by a United

States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

(B) *UNITED STATES AGENT REQUIRED.*—The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—

(i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or

(ii) any summons by the Secretary for such records or testimony.

The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints an agent described in this subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

(C) *OTHER RULES TO APPLY.*—Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.

(c) *REPORTING BY UNITED STATES BENEFICIARIES OF FOREIGN TRUSTS.*—

(1) *IN GENERAL.*—If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—

(A) the name of such trust,

(B) the aggregate amount of the distributions so received from such trust during such taxable year, and

(C) such other information as the Secretary may prescribe.

(2) *INCLUSION IN INCOME IF RECORDS NOT PROVIDED.*—

(A) *IN GENERAL.*—If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To the extent provided in regulations, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b)(2)(B).

(B) *APPLICATION OF ACCUMULATION DISTRIBUTION RULES.*—For purposes of applying section 668 in a case to which subparagraph (A) applies, the applicable number of years for purposes of section 668(a) shall be $\frac{1}{2}$ of the number of years the trust has been in existence.

(d) SPECIAL RULES.—

(1) DETERMINATION OF WHETHER UNITED STATES PERSON MAKES TRANSFER OR RECEIVES DISTRIBUTION.—For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

(2) DOMESTIC TRUSTS WITH FOREIGN ACTIVITIES.—To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

(3) TIME AND MANNER OF FILING INFORMATION.—Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

(4) MODIFICATION OF RETURN REQUIREMENTS.—The Secretary is authorized to suspend or modify any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.

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CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, AND ASSESSABLE PENALTIES

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Subchapter B—Assessable Penalties

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PART I—GENERAL PROVISIONS

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[Sec. 6677. Failure to file information returns with respect to certain foreign trusts.]

Sec. 6677. Failure to file information with respect to certain foreign trusts.

* * * * *

[SEC. 6677. FAILURE TO FILE INFORMATION RETURNS WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

[(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, any person required to file a return under section 6048 who fails to file such return at the time provided in such section, or who files a return which does not show the information required pursuant to such section, shall pay a penalty equal to 5 percent of the amount transferred to a trust (or, in the case of a failure with respect to section 6048(c), equal to 5 percent of the value of the corpus of the trust at the close of the taxable year), but not more than \$1,000, unless it is shown that such failure is due to reasonable cause.

[(b) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).**]**

SEC. 6677. FAILURE TO FILE INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

(a) *CIVIL PENALTY.—In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—*

(1) is not filed on or before the time provided in such section,

or

(2) does not include all the information required pursuant to such section or includes incorrect information,

the person required to file such notice or return shall pay a penalty equal to 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of \$10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of such 90-day period. In no event shall the penalty under this subsection with respect to any failure exceed the gross reportable amount.

(b) *SPECIAL RULES FOR RETURNS UNDER SECTION 6048(b).—In the case of a return required under section 6048(b)—*

(1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and

(2) subsection (a) shall be applied by substituting “5 percent” for “35 percent”.

(c) *GROSS REPORTABLE AMOUNT.—For purposes of subsection (a), the term “gross reportable amount” means—*

(1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),

(2) the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and

(3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

(d) *REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information is not reasonable cause.*

(e) *DEFICIENCY PROCEDURES NOT TO APPLY.—*Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).

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PART II—FAILURE TO COMPLY WITH CERTAIN INFORMATION REPORTING REQUIREMENTS

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SEC. 6724. WAIVER; DEFINITIONS AND SPECIAL RULES.

(a) * * *

* * * * *

(d) DEFINITIONS.—For purposes of this part—

(1) * * *

(2) PAYEE STATEMENT.—The term “payee statement” means any statement required to be furnished under—

(A) * * *

* * * * *

(S) section 6053(b) or (c) (relating to reports of tips), [or] (T) section 4093(c)(4)(B) (relating to certain purchasers of diesel and aviation fuels)[.], or (U) section 6048(b)(1)(B) (relating to foreign trust reporting requirements).

Such term also includes any form, statement, or schedule required to be furnished to the recipient of any amount from which tax was required to be deducted and withheld under chapter 3 (or from which tax would be required to be so deducted and withheld but for an exemption under this title or any treaty obligation of the United States).

* * * * *

CHAPTER 79—DEFINITIONS

* * * * *

SEC. 7701. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

(1) * * *

* * * * *

(30) UNITED STATES PERSON.—The term “United States person” means—

- (A) a citizen or resident of the United States,
- (B) a domestic partnership,
- (C) a domestic corporation, [and]

[(D) any estate or trust (other than a foreign estate or foreign trust, within the meaning of section 7701(a)(31)).]

(D) any estate (other than a foreign estate, within the meaning of paragraph (31)), and

(E) any trust if—

(i) a court within the United States is able to exercise primary supervision over the administration of the trust, and

(ii) one or more United States fiduciaries have the authority to control all substantial decisions of the trust.

[(31) FOREIGN ESTATE OR TRUST.—The terms “foreign estate” and “foreign trust” mean an estate or trust, as the case may be, the income of which, from sources without the United States which is not effectively connected with the conduct of a

trade or business within the United States, is not includible in gross income under subtitle A.】

(31) FOREIGN ESTATE OR TRUST.—

(A) FOREIGN ESTATE.—The term “foreign estate” means an estate the income of which, from sources without the United States which is not effectively connected with the conduct of a trade or business within the United States, is not includible in gross income under subtitle A.

(B) FOREIGN TRUST.—The term “foreign trust” means any trust other than a trust described in subparagraph (E) of paragraph (30).

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CHAPTER 80—GENERAL RULES

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Subchapter C—Provisions Affecting More Than One Substitute

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SEC. 7872. TREATMENT OF LOANS WITH BELOW-MARKET INTEREST RATES.

(a) * * *

* * * * *

(f) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * *

(8) LOANS TO WHICH SECTION 483, 643(i), OR 1274 APPLIES.—This section shall not apply to any loan to which section 483, 643(i), or 1274 applies.

* * * * *

SOCIAL SECURITY ACT

* * * * *

TITLE IV—GRANTS TO STATES FOR AID AND SERVICES TO NEEDY FAMILIES WITH CHILDREN AND FOR CHILD-WELFARE SERVICES

* * * * *

PART E—FEDERAL PAYMENTS FOR FOSTER CARE AND ADOPTION ASSISTANCE

* * * * *

STATE PLAN FOR FOSTER CARE AND ADOPTION ASSISTANCE

SEC. 471. (a) In order for a State to be eligible for payments under this part, it shall have a plan approved by the Secretary which—

(1) * * *

* * * * *

(16) provides for the development of a case plan (as defined in section 475(1)) for each child receiving foster care maintenance payments under the State plan and provides for a case review system which meets the requirements described in section 475(5)(B) with respect to each such child; [and]

(17) provides that, where appropriate, all steps will be taken, including cooperative efforts with the State agencies administering the plans approved under parts A and D, to secure an assignment to the State of any rights to support on behalf of each child receiving foster care maintenance payments under this part[.]; and

(18) not later than January 1, 1997, provides that neither the State nor any other entity in the State that receives funds from the Federal Government and is involved in adoption or foster care placements may—

(A) deny to any person the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the person, or of the child, involved; or

(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.

* * * * *

PAYMENTS TO STATES; ALLOTMENTS TO STATES

SEC. 474. (a) * * *

* * * * *

(d)(1) If a State's program operated under this part is found, as a result of a review conducted under section 1123, to have violated section 471(a)(18) during a quarter with respect to any person, then, notwithstanding subsection (a) of this section and any regulations promulgated under section 1123(b)(3), the Secretary shall reduce the amount otherwise payable to the State under this part, for the quarter and for each subsequent quarter before the 1st quarter for which the State program is found, as a result of such a review, not to have violated section 471(a)(18) with respect to any person, by—

(A) 2 percent of such otherwise payable amount, in the case of the 1st such finding with respect to the State;

(B) 5 percent of such otherwise payable amount, in the case of the 2nd such finding with respect to the State; or

(C) 10 percent of such otherwise payable amount, in the case of the 3rd or subsequent such finding with respect to the State.

(2) Any other entity which is in a State that receives funds under this part and which violates section 471(a)(18) during a quarter with respect to any person shall remit to the Secretary all funds that

were paid by the State to the entity during the quarter from such funds.

(3)(A) Any individual who is aggrieved by a violation of section 471(a)(18) by a State or other entity may bring an action seeking relief from the State or other entity in any United States district court.

(B) An action under this paragraph may not be brought more than 2 years after the date the alleged violation occurred.

(4) This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.

* * * * *

SECTION 553 OF THE HOWARD M. METZENBAUM MULTIETHNIC PLACEMENT ACT OF 1994

[(SEC. 553. MULTIETHNIC PLACEMENTS.

[(a) ACTIVITIES.—

[(1) PROHIBITION.—An agency, or entity, that receives Federal assistance and is involved in adoption or foster care placements may not—

[(A) categorically deny to any person the opportunity to become an adoptive or a foster parent, solely on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved; or

[(B) delay or deny the placement of a child for adoption or into foster care, or otherwise discriminate in making a placement decision, solely on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.

[(2) PERMISSIBLE CONSIDERATION.—An agency or entity to which paragraph (1) applies may consider the cultural, ethnic, or racial background of the child and the capacity of the prospective foster or adoptive parents to meet the needs of a child of this background as one of a number of factors used to determine the best interests of a child.

[(3) DEFINITION.—As used in this subsection, the term “placement decision” means the decision to place, or to delay or deny the placement of, a child in a foster care or an adoptive home, and includes the decision of the agency or entity involved to seek the termination of birth parent rights or otherwise make a child legally available for adoptive placement.

[(b) EQUITABLE RELIEF.—Any individual who is aggrieved by an action in violation of subsection (a), taken by an agency or entity described in subsection (a), shall have the right to bring an action seeking relief in a United States district court of appropriate jurisdiction.

[(c) FEDERAL GUIDANCE.—Not later than 6 months after the date of the enactment of this Act, the Secretary of Health and Human Services shall publish guidance to concerned public and private agencies and entities with respect to compliance with this subpart.

[(d) DEADLINE FOR COMPLIANCE.—

[(1) IN GENERAL.—Except as provided in paragraph (2), an agency or entity that receives Federal assistance and is in-

involved with adoption or foster care placements shall comply with this subpart not later than six months after publication of the guidance referred to in subsection (c), or one year after the date of enactment of this Act, whichever occurs first.

[(2) **AUTHORITY TO EXTEND DEADLINE.**—If a State demonstrates to the satisfaction of the Secretary that it is necessary to amend State statutory law in order to change a particular practice that is inconsistent with this subpart, the Secretary may extend the compliance date for the State a reasonable number of days after the close of the first State legislative session beginning after the date the guidance referred to in subsection (c) is published.

[(e) **NONCOMPLIANCE DEEMED A CIVIL RIGHTS VIOLATION.**—Non-compliance with this subpart is deemed a violation of title VI of the Civil Rights Act of 1964.

[(f) **NO EFFECT ON INDIAN CHILD WELFARE ACT OF 1978.**—Nothing in this section shall be construed to affect the application of the Indian Child Welfare Act of 1978 (25 U.S.C. 1901 et seq.).]

INDIAN CHILD WELFARE ACT OF 1978

* * * * *

TITLE I—CHILD CUSTODY PROCEEDINGS

* * * * *

SEC. 114. (a) This title does not apply to any child custody proceeding involving a child who does not reside or is not domiciled within a reservation unless—

(1) at least one of the child’s biological parents is of Indian descent; and

(2) at least one of the child’s biological parents maintains significant social, cultural, or political affiliation with the Indian tribe of which either parent is a member.

(b) The factual determination as to whether a biological parent maintains significant social, cultural, or political affiliation with the Indian tribe of which either parent is a member shall be based on such affiliation as of the time of the child custody proceeding.

(c) The determination that this title does not apply pursuant to subsection (a) is final, and, thereafter, this title shall not be the basis for determining jurisdiction over any child custody proceeding involving the child.

SEC. 115. (a) A person who attains the age of 18 years before becoming a member of an Indian tribe may become a member of an Indian tribe only upon the person’s written consent.

(b) For the purposes of any child custody proceeding involving an Indian child, membership in an Indian tribe shall be effective from the actual date of admission to membership in the Indian tribe and shall not be given retroactive effect.

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