

107TH CONGRESS
2^D SESSION

S. 2119

To amend the Internal Revenue Code of 1986 to provide for the tax treatment of inverted corporate entities and of transactions with such entities, and for other purposes.

IN THE SENATE OF THE UNITED STATES

APRIL 11, 2002

Mr. GRASSLEY (for himself and Mr. BAUCUS) introduced the following bill;
which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 to provide for the tax treatment of inverted corporate entities and of transactions with such entities, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Reversing the Expa-
5 triation of Profits Offshore Act”.

1 **SEC. 2. TAX TREATMENT OF INVERTED CORPORATE ENTI-**
 2 **TIES.**

3 (a) IN GENERAL.—Subchapter C of chapter 80 of the
 4 Internal Revenue Code of 1986 (relating to provisions af-
 5 fecting more than one subtitle) is amended by adding at
 6 the end the following new section:

7 **“SEC. 7874. RULES RELATING TO INVERTED CORPORATE**
 8 **ENTITIES.**

9 “(a) INVERTED CORPORATIONS TREATED AS DOMES-
 10 TIC CORPORATIONS.—

11 “(1) IN GENERAL.—If a foreign incorporated
 12 entity is treated as an inverted domestic corporation,
 13 then, notwithstanding section 7701(a)(4), such enti-
 14 ty shall be treated for purposes of this title as a do-
 15 mestic corporation.

16 “(2) INVERTED DOMESTIC CORPORATION.—For
 17 purposes of this section, a foreign incorporated enti-
 18 ty shall be treated as an inverted domestic corpora-
 19 tion if, pursuant to a plan (or a series of related
 20 transactions)—

21 “(A) the entity completes after March 20,
 22 2002, the direct or indirect acquisition of sub-
 23 stantially all of the properties held directly or
 24 indirectly by a domestic corporation or substan-
 25 tially all of the properties constituting a trade
 26 or business of a domestic partnership,

1 “(B) after the acquisition at least 80 per-
2 cent of the stock (by vote or value) of the entity
3 is held—

4 “(i) in the case of an acquisition with
5 respect to a domestic corporation, by
6 former shareholders of the domestic cor-
7 poration by reason of holding stock in the
8 domestic corporation, or

9 “(ii) in the case of an acquisition with
10 respect to a domestic partnership, by
11 former partners of the domestic partner-
12 ship, and

13 “(C) the expanded affiliated group which
14 after the acquisition includes the entity does
15 not have substantial business activities in the
16 foreign country in which or under the law of
17 which the entity is created or organized when
18 compared to the total business activities of such
19 expanded affiliated group.

20 “(b) PRESERVATION OF DOMESTIC TAX BASE IN
21 CERTAIN INVERSION TRANSACTIONS TO WHICH SUB-
22 SECTION (a) DOES NOT APPLY.—

23 “(1) IN GENERAL.—If a foreign incorporated
24 entity would be treated as an inverted domestic cor-

1 poration with respect to an acquired entity if
2 either—

3 “(A) subsection (a)(2)(A) were applied by
4 substituting ‘on or before March 20, 2002’ for
5 ‘after March 20, 2002’ and subsection
6 (a)(2)(B) were applied by substituting ‘more
7 than 50 percent’ for ‘at least 80 percent’, or

8 “(B) subsection (a)(2)(B) were applied by
9 substituting ‘more than 50 percent’ for ‘at least
10 80 percent’,

11 then the rules of subsection (c) shall apply to any
12 inversion gain of the acquired entity during the ap-
13 plicable period and the rules of subsection (d) shall
14 apply to any related party transaction of the ac-
15 quired entity during the applicable period. This sub-
16 section shall not apply for any taxable year if sub-
17 section (a) applies to such foreign incorporated enti-
18 ty for such taxable year.

19 “(2) ACQUIRED ENTITY.—For purposes of this
20 section—

21 “(A) IN GENERAL.—The term ‘acquired
22 entity’ means the domestic corporation or part-
23 nership substantially all of the properties of
24 which are directly or indirectly acquired in an

1 acquisition described in subsection (a)(2)(A) to
2 which this subsection applies.

3 “(B) AGGREGATION RULES.—Any domes-
4 tic person bearing a relationship described in
5 section 267(b) or 707(b) to an acquired entity
6 shall be treated as an acquired entity with re-
7 spect to the acquisition described in subpara-
8 graph (A).

9 “(3) APPLICABLE PERIOD.—For purposes of
10 this section—

11 “(A) IN GENERAL.—The term ‘applicable
12 period’ means the period—

13 “(i) beginning on the first date prop-
14 erties are acquired as part of the acquisi-
15 tion described in subsection (a)(2)(A) to
16 which this subsection applies, and

17 “(ii) ending on the date which is 10
18 years after the last date properties are ac-
19 quired as part of such acquisition.

20 “(B) SPECIAL RULE FOR INVERSIONS OC-
21 CURRING BEFORE MARCH 21, 2002.—In the case
22 of any acquired entity to which paragraph
23 (1)(A) applies, the applicable period shall be the
24 10-year period beginning on January 1, 2002.

1 “(c) TAX ON INVERSION GAINS MAY NOT BE OFF-
2 SET.—If subsection (b) applies—

3 “(1) IN GENERAL.—The taxable income of an
4 acquired entity for any taxable year which includes
5 any portion of the applicable period shall in no event
6 be less than the inversion gain of the entity for the
7 taxable year.

8 “(2) CREDITS NOT ALLOWED AGAINST TAX ON
9 INVERSION GAIN.—Credits shall be allowed against
10 the tax imposed by chapter 1 on an acquired entity
11 for any taxable year described in paragraph (1) only
12 to the extent such tax exceeds the product of—

13 “(A) the amount of taxable income de-
14 scribed in paragraph (1) for the taxable year,
15 and

16 “(B) the highest rate of tax specified in
17 section 11(b)(1).

18 “(3) SPECIAL RULES FOR PARTNERSHIPS.—In
19 the case of an acquired entity which is a
20 partnership—

21 “(A) the limitations of this subsection shall
22 apply at the partner rather than the partner-
23 ship level,

24 “(B) the inversion gain of any partner for
25 any taxable year shall be equal to the sum of—

1 “(i) the partner’s distributive share of
2 inversion gain of the partnership for such
3 taxable year, plus

4 “(ii) gain required to be recognized
5 for the taxable year by the partner under
6 section 367(a), 741, or 1001, or under any
7 other provision of chapter 1, by reason of
8 the transfer during the applicable period of
9 any partnership interest of the partner in
10 such partnership to the foreign incor-
11 porated entity, and

12 “(C) the highest rate of tax specified in
13 the rate schedule applicable to the partner
14 under chapter 1 shall be substituted for the
15 rate of tax under paragraph (2)(B).

16 “(4) INVERSION GAIN.—For purposes of this
17 section, the term ‘inversion gain’ means the gain re-
18 quired to be recognized under section 304, 311(b),
19 367, 1001, or 1248, or under any other provision of
20 chapter 1, by reason of the transfer during the ap-
21 plicable period of stock or other properties by an ac-
22 quired entity—

23 “(A) as part of the acquisition described in
24 subsection (a)(2)(A) to which subsection (b) ap-
25 plies, or

1 “(B) after such acquisition to a foreign re-
2 lated person.

3 “(5) COORDINATION WITH SECTION 172 AND
4 MINIMUM TAX.—Rules similar to the rules of para-
5 graphs (3) and (4) of section 860E(a) shall apply
6 for purposes of this subsection.

7 “(d) SPECIAL RULES APPLICABLE TO RELATED
8 PARTY TRANSACTIONS.—

9 “(1) ANNUAL PREAPPROVAL REQUIRED.—

10 “(A) IN GENERAL.—An acquired entity to
11 which subsection (b) applies shall enter into an
12 annual preapproval agreement under subpara-
13 graph (C) with the Secretary for each taxable
14 year which includes a portion of the applicable
15 period.

16 “(B) FAILURES TO ENTER AGREE-
17 MENTS.—If an acquired entity fails to meet the
18 requirements of subparagraph (A) for any tax-
19 able year, then for such taxable year—

20 “(i) there shall not be allowed any de-
21 duction, or addition to basis or cost of
22 goods sold, for amounts paid or incurred,
23 or losses incurred, by reason of a trans-
24 action between the acquired entity and a
25 foreign related person,

1 “(ii) any transfer or license of intan-
2 gible property (as defined in section
3 936(h)(3)(B)) between the acquired entity
4 and a foreign related person shall be dis-
5 regarded, and

6 “(iii) any cost-sharing arrangement
7 between the acquired entity and a foreign
8 related person shall be disregarded.

9 “(C) PREAPPROVAL AGREEMENT.—For
10 purposes of subparagraph (A), the term
11 ‘preapproval agreement’ means a prefilling, ad-
12 vance pricing, or other agreement specified by
13 the Secretary which—

14 “(i) is entered into at such time as
15 may be specified by the Secretary, and

16 “(ii) contains such provisions as the
17 Secretary determines necessary to ensure
18 that the requirements of sections 163(j),
19 267(a)(3), 482, and 845, and any other
20 provision of this title applicable to trans-
21 actions between related persons and speci-
22 fied by the Secretary, are met.

23 “(2) MODIFICATIONS OF LIMITATION ON INTER-
24 EST DEDUCTION.—In the case of an acquired entity

1 to which subsection (b) applies, section 163(j) shall
2 be applied—

3 “(A) without regard to paragraph
4 (2)(A)(ii) thereof, and

5 “(B) by substituting ‘25 percent’ for ‘50
6 percent’ each place it appears in paragraph
7 (2)(B) thereof.

8 “(e) OTHER DEFINITIONS AND SPECIAL RULES.—
9 For purposes of this section—

10 “(1) RULES FOR APPLICATION OF SUBSECTION
11 (a)(2).—In applying subsection (a)(2) for purposes of
12 subsections (a) and (b), the following rules shall
13 apply:

14 “(A) CERTAIN STOCK DISREGARDED.—
15 There shall not be taken into account in deter-
16 mining ownership for purposes of subsection
17 (a)(2)(B)—

18 “(i) stock held by members of the ex-
19 panded affiliated group which includes the
20 foreign incorporated entity, or

21 “(ii) stock of such entity which is sold
22 in a public offering related to the acquisi-
23 tion described in subsection (a)(2)(A).

24 “(B) PLAN DEEMED IN CERTAIN CASES.—
25 If a foreign incorporated entity acquires directly

1 or indirectly substantially all of the properties
2 of a domestic corporation or partnership during
3 the 4-year period beginning on the date which
4 is 2 years before the ownership requirements of
5 subsection (a)(2)(B) are met, such actions shall
6 be treated as pursuant to a plan.

7 “(C) CERTAIN TRANSFERS DIS-
8 REGARDED.—The transfer of properties or li-
9 abilities (including by contribution or distribu-
10 tion) shall be disregarded if such transfers are
11 part of a plan a principal purpose of which is
12 to avoid the purposes of this section.

13 “(D) SPECIAL RULE FOR RELATED PART-
14 NERSHIPS.—For purposes of applying sub-
15 section (a)(2) to the acquisition of a domestic
16 partnership, except as provided in regulations,
17 all partnerships which are under common con-
18 trol (within the meaning of section 482) shall
19 be treated as 1 partnership.

20 “(2) EXPANDED AFFILIATED GROUP.—The
21 term ‘expanded affiliated group’ means an affiliated
22 group as defined in section 1504(a) but without re-
23 gard to section 1504(b), except that section 1504(a)
24 shall be applied by substituting ‘more than 50 per-
25 cent’ for ‘at least 80 percent’ each place it appears.

1 “(3) FOREIGN INCORPORATED ENTITY.—The
2 term ‘foreign incorporated entity’ means any entity
3 which is, or but for subsection (a)(1) would be,
4 treated as a foreign corporation for purposes of this
5 title.

6 “(4) FOREIGN RELATED PERSON.—The term
7 ‘foreign related person’ means, with respect to any
8 acquired entity, a foreign person which—

9 “(A) bears a relationship to such entity de-
10 scribed in section 267(b) or 707(b), or

11 “(B) is under the same common control
12 (within the meaning of section 482) as such en-
13 tity.

14 “(f) REGULATIONS.—The Secretary shall provide
15 such regulations as are necessary to carry out this section,
16 including regulations providing for such adjustments to
17 the application of this section as are necessary to prevent
18 the avoidance of the purposes of this section, including the
19 avoidance of such purposes through—

20 “(1) the use of related persons, pass-through or
21 other noncorporate entities, or other intermediaries,
22 or

23 “(2) transactions designed to have persons
24 cease to be (or not become) members of expanded
25 affiliated groups or related persons.”.

1 (b) TREATMENT OF AGREEMENTS.—

2 (1) CONFIDENTIALITY.—

3 (A) TREATMENT AS RETURN INFORMA-
4 TION.—Section 6103(b)(2) of the Internal Rev-
5 enue Code of 1986 (relating to return informa-
6 tion) is amended by striking “and” at the end
7 of subparagraph (C), by inserting “and” at the
8 end of subparagraph (D), and by inserting after
9 subparagraph (D) the following new subpara-
10 graph:

11 “(E) any preapproval agreement under
12 section 7874(d)(1) to which any preceding sub-
13 paragraph does not apply and any background
14 information related to the agreement or any ap-
15 plication for the agreement,”.

16 (B) EXCEPTION FROM PUBLIC INSPECTION
17 AS WRITTEN DETERMINATION.—Section
18 6110(b)(1)(B) of such Code is amended by
19 striking “or (D)” and inserting “, (D), or (E)”.

20 (2) REPORTING.—The Secretary of the Treas-
21 ury shall include with any report on advance pricing
22 agreements required to be submitted after the date
23 of the enactment of this Act under section 521(b) of
24 the Ticket to Work and Work Incentives Improve-
25 ment Act of 1999 (Public Law 106–170) a report

1 regarding preapproval agreements under section
 2 7874(d)(1) of the Internal Revenue Code of 1986.
 3 Such report shall include information similar to the
 4 information required with respect to advance pricing
 5 agreements and shall be treated for confidentiality
 6 purposes in the same manner as the reports on ad-
 7 vance pricing agreements are treated under section
 8 521(b)(3) of such Act.

9 (c) CONFORMING AMENDMENTS.—The table of sec-
 10 tions for subchapter C of chapter 80 of the Internal Rev-
 11 enue Code of 1986 is amended by adding at the end the
 12 following new item:

“Sec. 7874. Rules relating to inverted corporate entities.”

13 **SEC. 3. REINSURANCE OF UNITED STATES RISKS IN FOR-**
 14 **EIGN JURISDICTIONS.**

15 (a) IN GENERAL.—Section 845(a) of the Internal
 16 Revenue Code of 1986 (relating to allocation in case of
 17 reinsurance agreement involving tax avoidance or evasion)
 18 is amended by striking “source and character” and insert-
 19 ing “amount, source, or character”.

20 (b) EFFECTIVE DATE.—The amendments made by
 21 this section shall apply to any risk reinsured after April
 22 11, 2002.

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