

[WAYS AND MEANS DISCUSSION DRAFT]

JANUARY 23, 2013

113TH CONGRESS
1ST SESSION

H. R. _____

To amend the Internal Revenue Code of 1986 to provide for comprehensive income tax reform.

IN THE HOUSE OF REPRESENTATIVES

M. _____ introduced the following bill; which was referred to the Committee on _____

A BILL

To amend the Internal Revenue Code of 1986 to provide for comprehensive income tax reform.

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; ETC.**

4 (a) SHORT TITLE.—This Act may be cited as the
5 “Tax Reform Act of 2013”.

6 (b) AMENDMENT OF 1986 CODE.—Except as other-
7 wise expressly provided, whenever in this Act an amend-
8 ment or repeal is expressed in terms of an amendment

1 to, or repeal of, a section or other provision, the reference
2 shall be considered to be made to a section or other provi-
3 sion of the Internal Revenue Code of 1986.

4 (c) TABLE OF CONTENTS.—The table of contents of
5 this Act is as follows:

Sec. 1. Short title; etc.

TITLE I—TAX REFORM FOR INDIVIDUALS

Sec. 101. [to be provided].

TITLE II—TAX REFORM FOR BUSINESSES

Sec. 201. [to be provided].

TITLE III—PARTICIPATION EXEMPTION SYSTEM FOR THE
TAXATION OF FOREIGN INCOME

Sec. 301. [to be provided].

TITLE IV—OTHER REFORMS

Subtitle A—Financial Instruments

PART 1—DERIVATIVES AND HEDGES

Sec. 401. Treatment of derivatives.

Sec. 402. Treatment of hedges identified for financial accounting purposes.

PART 2—TREATMENT OF DISCOUNT AND PREMIUM

Sec. 411. Determination of issue price in the case of specified debt modifica-
tions.

Sec. 412. Deduction for amortizable bond premium allowed in determining ad-
justed gross income.

Sec. 413. Current inclusion in income of market discount.

Sec. 414. Rules regarding certain government debt.

PART 3—CERTAIN RULES FOR DETERMINING GAIN AND LOSS

Sec. 421. Cost basis of specified securities determined in accordance with aver-
age basis method.

Sec. 422. Wash sales by related parties.

Subtitle B—[additional Reforms to Be Provided]

1 **TITLE I—TAX REFORM FOR**
2 **INDIVIDUALS**

3 **SEC. 101. [TO BE PROVIDED].**

4 **TITLE II—TAX REFORM FOR**
5 **BUSINESSES**

6 **SEC. 201. [TO BE PROVIDED].**

7 **TITLE III—PARTICIPATION EX-**
8 **EMPTION SYSTEM FOR THE**
9 **TAXATION OF FOREIGN IN-**
10 **COME**

11 **SEC. 301. [TO BE PROVIDED].**

12 **TITLE IV—OTHER REFORMS**
13 **Subtitle A—Financial Instruments**

14 **PART 1—DERIVATIVES AND HEDGES**

15 **SEC. 401. TREATMENT OF DERIVATIVES.**

16 (a) IN GENERAL.—Subchapter E of chapter 1 is
17 amended by adding at the end the following new part:

18 **“PART IV—DERIVATIVES**

 “Sec. 485. Treatment of derivatives.

 “Sec. 486. Derivative defined.

19 **“SEC. 485. TREATMENT OF DERIVATIVES.**

20 “(a) GENERAL RULE.—For purposes of this sub-
21 title—

22 “(1) any derivative held by a taxpayer at the
23 close of the taxable year shall be treated as sold for
24 its fair market value on the last business day of

1 such taxable year (and any gain or loss shall be
2 taken into account for the taxable year), and

3 “(2) proper adjustment shall be made in the
4 amount of any gain or loss subsequently realized for
5 gain or loss taken into account by reason of para-
6 graph (1).

7 “(b) TREATMENT AS ORDINARY INCOME OR LOSS;
8 ALLOWANCE AS NET OPERATING LOSS.—All items of in-
9 come, gain, loss, and deduction with respect to such deriv-
10 ative—

11 “(1) shall be treated as ordinary income or loss,
12 and

13 “(2) shall be treated for purposes of section
14 172(d)(4) as attributable to a trade or business of
15 the taxpayer.

16 “(c) MARK TO MARKET OF ALL POSITIONS IN MIXED
17 STRADDLES.—

18 “(1) IN GENERAL.—In the case of any straddle
19 which includes any derivative to which subsection (a)
20 applies, subsections (a) and (b) shall apply to all po-
21 sitions in such straddle in the same manner as such
22 subsections apply to such derivative.

23 “(2) SPECIAL RULES FOR BUILT-IN GAIN POSI-
24 TIONS.—

1 “(A) IN GENERAL.—In the case of any
2 built-in gain position to which paragraph (1)
3 applies—

4 “(i) in addition to any other time at
5 which such position is treated as sold
6 under subsection (a)(1), such position shall
7 be treated as sold as provided in subsection
8 (a)(1) at the time that the straddle is es-
9 tablished with respect to such position, and

10 “(ii) subsection (b) shall not apply to
11 any gain taken into account by reason of
12 clause (i).

13 “(B) BUILT-IN GAIN POSITION.—For pur-
14 poses of subparagraph (A), the term ‘built-in
15 gain position’ means any position (other than a
16 derivative to which subsection (a) applies) with
17 respect to which a gain would be realized if
18 such position were sold for its fair market value
19 at the time that the straddle is established with
20 respect to such position.

21 “(3) SPECIAL RULES FOR BUILT-IN LOSS POSI-
22 TIONS.—

23 “(A) IN GENERAL.—In the case of any
24 built-in loss position to which paragraph (1) ap-
25 plies, any gain or loss realized under subsection

1 (a)(1) shall be properly adjusted so as not to
2 take into account the loss referred to in sub-
3 paragraph (B) with respect to such position.

4 “(B) BUILT-IN LOSS POSITION.—For pur-
5 poses of subparagraph (A), the term ‘built-in
6 loss position’ means any position (other than a
7 derivative to which subsection (a) applies) with
8 respect to which a loss would be realized if such
9 position were sold for its fair market value at
10 the time that the straddle is established with
11 respect to such position.

12 “(4) SUSPENSION OF HOLDING PERIODS FOR
13 NON-DERIVATIVES.—In the case of any position to
14 which paragraph (1) applies, the holding period of
15 such position shall not include any period during
16 which such position is part of such straddle.

17 “(5) STRADDLE.—For purposes of this sec-
18 tion—

19 “(A) the term ‘straddle’ has the meaning
20 given such term by section 1092(c) applied
21 without regard to paragraph (2)(B) thereof and
22 by treating all offsetting positions as being with
23 respect to personal property, and

24 “(B) the term ‘position’ includes any deriv-
25 ative.

1 “(d) TERMINATIONS, ETC.—

2 “(1) IN GENERAL.—The rules of subsections
3 (a) and (b) shall also apply to the termination (or
4 transfer) during the taxable year of the taxpayer’s
5 obligation (or rights) with respect to a derivative by
6 offsetting, by taking or making delivery, by exercise
7 or being exercised, by assignment or being assigned,
8 by lapse, by expiration, by settlement, or otherwise.

9 “(2) SPECIAL RULE FOR STRADDLES.—If para-
10 graph (1) applies with respect to any position which
11 is part of a straddle, the rules of subsections (a) and
12 (b) shall apply to every position which is part of
13 such straddle.

14 “(e) DETERMINATION OF FAIR MARKET VALUE.—
15 For purposes of this section—

16 “(1) FAIR MARKET VALUE NOT READILY AS-
17 CERTAINABLE.—To the extent provided in regula-
18 tions prescribed by the Secretary, where there is no
19 readily ascertainable fair market value, fair market
20 value shall be determined under the method used for
21 the purpose of a report or statement—

22 “(A) to shareholders, partners, or other
23 proprietors, to beneficiaries, or to such other
24 persons as the Secretary may specify in such
25 regulations, or

1 “(B) for credit purposes.

2 “(2) TERMINATIONS, ETC.—For purposes of
3 subsection (d), fair market value shall be determined
4 at the time of the termination (or transfer).

5 “(3) CONVERTIBLE INSTRUMENTS WITH EM-
6 BDED DERIVATIVE COMPONENTS.—The fair mar-
7 ket value of an embedded derivative component (as
8 defined in section 486) shall be the excess of—

9 “(A) the fair market value of the debt in-
10 strument including such component, over

11 “(B) the fair market value of the debt in-
12 strument not including such component.

13 “(4) BLOCKAGE FACTOR NOT TAKEN INTO AC-
14 COUNT.—To the extent provided in regulations pre-
15 scribed by the Secretary, fair market value shall be
16 determined without regard to any premium or dis-
17 count based on the proportion of the total available
18 trading units which are held.

19 **“SEC. 486. DERIVATIVE DEFINED.**

20 “(a) IN GENERAL.—For purposes of this part, except
21 as otherwise provided in this section, the term ‘derivative’
22 means—

23 “(1) any evidence of an interest in (or any de-
24 rivative financial instrument with respect to)—

25 “(A) any share of stock in a corporation,

1 “(B) any partnership or beneficial owner-
2 ship interest in a partnership or trust,

3 “(C) any note, bond, debenture, or other
4 evidence of indebtedness,

5 “(D) except as provided in subsection (e),
6 any real property,

7 “(E) any commodity which is actively trad-
8 ed (within the meaning of section 1092(d)(1)),
9 or

10 “(F) any currency,

11 “(2) any notional principal contract, and

12 “(3) any derivative financial instrument with
13 respect to any interest or instrument described in
14 paragraph (1) or (2) (or this paragraph).

15 “(b) DERIVATIVE FINANCIAL INSTRUMENT.—For
16 purposes of this section, the term ‘derivative financial in-
17 strument’ includes any option, forward contract, futures
18 contract, short position, swap, or similar financial instru-
19 ment

20 “(c) NOTIONAL PRINCIPAL CONTRACT.—For pur-
21 poses of this section—

22 “(1) IN GENERAL.—Except as otherwise pro-
23 vided by the Secretary, the term ‘notional principal
24 contract’ means any financial instrument which re-
25 quires two or more payments at specified intervals

1 calculated by reference to a specified index upon one
2 or more notional principal amounts. An amount
3 shall not fail to be treated as a payment described
4 in the preceding sentence merely because such
5 amount is fixed on one date and paid or otherwise
6 taken into account on a different date.

7 “(2) SPECIFIED INDEX.—For purposes of this
8 subsection, the term ‘specified index’ means any one
9 or more of (or any combination of)—

10 “(A) a rate, price, or amount (whether
11 fixed or variable),

12 “(B) any index based on any information
13 (including the occurrence or nonoccurrence of
14 any event) which is not within the control of
15 any of the parties to the instrument and is not
16 unique to any of the parties’ circumstances, and

17 “(C) any other index as the Secretary may
18 prescribe.

19 “(d) DEBT INSTRUMENTS HAVING EMBEDDED DE-
20 RIVATIVE COMPONENTS.—

21 “(1) IN GENERAL.—For purposes of this part,
22 the term ‘derivative’ includes any embedded deriva-
23 tive component.

24 “(2) EMBEDDED DERIVATIVE COMPONENT.—

25 For purposes of this section—

1 “(A) IN GENERAL.—The term ‘embedded
2 derivative component’ means any terms of a
3 debt instrument that affect some or all of the
4 cash flows or the value of other payments re-
5 quired by the instrument in a manner similar to
6 a derivative. Such component and the debt in-
7 strument shall be treated as two separate in-
8 struments for purposes of this part.

9 “(B) EXCEPTIONS.—A debt instrument
10 shall not be treated as having an embedded de-
11 rivative component merely because—

12 “(i) such debt instrument is denomi-
13 nated in a nonfunctional currency (as de-
14 fined in section 988(c)(1)(C)(ii)),

15 “(ii) payments with respect to such
16 debt instrument are determined by ref-
17 erence to the value of a nonfunctional cur-
18 rency (as so defined), or

19 “(iii) such debt instrument is a con-
20 tingent payment debt instrument, variable
21 rate debt instrument, or a debt instrument
22 with alternative payment schedules.

23 “(e) EXCEPTION FOR CERTAIN REAL PROPERTY.—

1 “(1) IN GENERAL.—An interest or instrument
2 shall not be treated as described in subsection
3 (a)(1)(D) if—

4 “(A) such interest or instrument is with
5 respect to a tract of real property (as defined
6 in section 1237(c)), or

7 “(B) such interest or instrument is with
8 respect to only real property which would be in-
9 ventory in the hands of the taxpayer if held di-
10 rectly by the taxpayer.

11 “(2) REGULATIONS.—The Secretary shall pre-
12 scribe regulations or other guidance under which
13 multiple tracts of real property may be treated as a
14 single tract of real property for purposes of para-
15 graph (1)(A) if the interest or instrument is of a
16 type which is designed to facilitate the acquisition or
17 disposition of such real property.

18 “(f) EXCEPTION FOR HEDGING TRANSACTIONS.—

19 “(1) IN GENERAL.—Section 485 shall not apply
20 to any financial instrument or other contract which
21 is part of a hedging transaction (as defined in sec-
22 tion 1221(c)).

23 “(2) SECTION 988 HEDGING TRANSACTIONS.—
24 For exception for section 988 hedging transactions,
25 see section 988(d)(1).”.

1 (b) COORDINATION WITH RULES FOR DEALERS AND
2 TRADERS.—

3 (1) DERIVATIVES NOT TREATED AS SECURI-
4 TIES.—Section 475(c)(2) is amended—

5 (A) by adding “and” at the end of sub-
6 paragraph (C),

7 (B) by striking subparagraphs (D) and (E)
8 and by redesignating subparagraph (F) as sub-
9 paragraph (D),

10 (C) by striking “subparagraph (A), (B),
11 (C), (D), or (E)” in subparagraph (D)(i), as so
12 redesignated, and inserting “subparagraph (A),
13 (B), or (C)”, and

14 (D) by amending the last sentence to read
15 as follows: “Such term shall not include any po-
16 sition to which section 485(a) applies.”

17 (2) DERIVATIVES NOT TREATED AS COMMOD-
18 ITIES.—Section 475(e)(2) is amended—

19 (A) by adding “and” at the end of sub-
20 paragraph (A),

21 (B) by striking subparagraphs (B) and (C)
22 and by redesignating subparagraph (D) as sub-
23 paragraph (B), and

1 (C) by striking “subparagraph (A), (B) or
2 (C)” in subparagraph (B)(i), as so redesign-
3 nated, and inserting “subparagraph (A)”.

4 (3) CONFORMING AMENDMENTS.—

5 (A) Section 475(b) is amended by striking
6 paragraph (4).

7 (B) Section 475(d)(2)(B) is amended—

8 (i) by striking “subsection
9 (c)(2)(F)(iii)” and inserting “subsection
10 (c)(2)(D)(iii)”, and

11 (ii) by striking “subsection (c)(2)(F)”
12 and inserting “subsection (c)(2)(D)”.

13 (C) Section 475(f)(1)(D) is amended by
14 striking “subsections (b)(4) and (d)” and in-
15 sserting “subsection (d)”.

16 (c) COORDINATION WITH STRADDLE RULES.—

17 (1) IN GENERAL.—Section 1092(e) is amended
18 to read as follows:

19 “(e) EXCEPTION FOR HEDGING TRANSACTIONS AND
20 STRADDLES WITH DERIVATIVES.—This section shall not
21 apply in the case of—

22 “(1) any hedging transaction (as defined in sec-
23 tion 1221(c)), and

1 “(2) any straddle (as defined in section 485)
2 which includes any derivative (as defined in section
3 486).”.

4 (2) CONFORMING AMENDMENTS.—

5 (A) Section 263(g)(3) is amended to read
6 as follows:

7 “(3) EXCEPTION FOR HEDGING TRANSACTIONS
8 AND STRADDLES WITH DERIVATIVES.—This sub-
9 section shall not apply in the case of—

10 “(A) any hedging transaction (as defined
11 in section 1221(c)), and

12 “(B) any straddle (as defined in section
13 485) which includes any derivative (as defined
14 in section 486).”.

15 (B) Section 1092(b) is amended—

16 (i) by striking paragraph (2), and

17 (ii) by striking all that precedes “The
18 Secretary shall” and inserting the fol-
19 lowing:

20 “(b) REGULATIONS.—The Secretary shall”.

21 (C) Section 1092(c) is amended by striking
22 paragraph (4).

23 (D) Section 1092 is amended by striking
24 subsection (f).

1 (d) REPEAL OF CERTAIN OTHER SUPERCEDED
2 RULES FOR DETERMINING CAPITAL GAINS AND
3 LOSSES.—

4 (1) IN GENERAL.—Part IV of subchapter P of
5 chapter 1 is amended by striking sections 1234B,
6 1236, 1256, and (and by striking the items relating
7 to such sections in the table of sections for such
8 part).

9 (2) CONFORMING AMENDMENTS RELATED TO
10 REPEAL OF SECTION 1236.—

11 (A) Section 475(d)(3)(A) is amended by
12 striking “or section 1236(b)”.

13 (B) Section 512(b)(5) is amended by strik-
14 ing “section 1236(c)” and inserting “section
15 1058(c)”.

16 (C) Section 1058 is amended—

17 (i) by striking “(as defined in section
18 1236(c))” in subsection (a), and

19 (ii) by redesignating subsection (c) as
20 subsection (d) and by inserting after sub-
21 section (b) the following new subsection:

22 “(c) SECURITIES.—For purposes of this section, the
23 term ‘security’ means any share of stock in any corpora-
24 tion, certificate of stock or interest in any corporation,
25 note, bond, debenture, or evidence of indebtedness, or any

1 evidence of an interest in or right to subscribe to or pur-
2 chase any of the foregoing.”.

3 (3) CONFORMING AMENDMENTS RELATED TO
4 REPEAL OF SECTION 1256.—

5 (A) Section 461(i)(3)(B) is amended to
6 read as follows:

7 “(B) any partnership or other entity (other
8 than a corporation which is not an S corpora-
9 tion) if more than 35 percent of the losses of
10 such entity during the taxable year are allocable
11 to limited partners or limited entrepreneurs
12 (within the meaning of section 464(e)(2)),
13 and”.

14 (B) Section 475(d)(1) is amended by strik-
15 ing “sections 263(g), 263A, and 1256(a)” and
16 inserting “sections 263(g) and 263A”.

17 (C) Section 988(e)(1) is amended by strik-
18 ing subparagraphs (D) and (E).

19 (D) Section 1092(a)(3)(C)(ii)(II) is
20 amended by striking “section 1256(e)” and in-
21 sserting “section 1221(c)”.

22 (E) Section 1092(d) is amended by strik-
23 ing paragraphs (5) and (6) and by redesignig-
24 nating paragraphs (7) and (8) as paragraphs
25 (5) and (6), respectively.

1 (F) Section 1212 is amended by striking
2 subsection (c).

3 (G) Section 1223 is amended by striking
4 paragraphs (7) and (14).

5 (H) Section 1258(d)(5) is amended—

6 (i) by striking “section 1256 con-
7 tracts” in subparagraph (A)(ii) and insert-
8 ing “commodity futures contracts”, and

9 (ii) by inserting “as in effect before
10 its repeal” after “section 1256(g)(8)” in
11 subparagraph (B)(i).

12 (I) Section 1281(b)(1)(E) is amended to
13 read as follows:

14 “(E) is a hedging transaction (as defined
15 in section 1221(c)), or”.

16 (J) Section 1402 is amended by striking
17 subsection (i).

18 (K) Section 4982(e)(6)(B) is amended by
19 striking “sections 1256 and 1296” and insert-
20 ing “sections 485 and 1296”.

21 (e) OTHER CONFORMING AMENDMENTS.—

22 (1) Section 856(n)(4) is amended by inserting
23 “or derivatives (as defined in section 486)” after
24 “securities (as defined in section 475(c)(2))”.

25 (2) Section 988(d)(1) is amended—

1 (A) by striking “or 1256” and inserting
2 “or 485”, and

3 (B) by striking “1092, and 1256” and in-
4 serting “485, and 1092”.

5 (3) Section 1091(e) is amended to read as fol-
6 lows:

7 “(e) COORDINATION WITH MARK-TO-MARKET OF
8 DERIVATIVES.—Notwithstanding any other provision of
9 this section, a derivative (as defined in section 486) shall
10 not be treated as a security for purposes of this section.”.

11 (4)(A) Section 1221(a)(6) is amended to read
12 as follows:

13 “(6) any derivative (as defined in section
14 486),”.

15 (B) Section 1221(b) is amended by striking
16 paragraph (1).

17 (5) Section 4975(f)(11)(D) is amended by
18 striking clauses (i) and (ii) and inserting the fol-
19 lowing:

20 “(i) SECURITY.—The term ‘security’
21 means any security described in section
22 475(c)(2) (without regard to subparagraph
23 (D)(iii) thereof) and any derivative with re-
24 spect to such a security (within the mean-
25 ing of section 486).

1 “(ii) COMMODITY.—The term ‘com-
2 modity’ means any commodity described in
3 section 475(e)(2) (without regard to sub-
4 paragraph (B)(iii) thereof) and any deriva-
5 tive with respect to such a commodity
6 (within the meaning of section 486).”.

7 (6) The table of parts for subchapter E of
8 chapter 1 is amended by adding at the end the fol-
9 lowing new item:

PART IV. DERIVATIVES.

10 (f) EFFECTIVE DATE.—The amendments made by
11 this section shall apply to property acquired and positions
12 established after December 31, 2013.

13 **SEC. 402. TREATMENT OF HEDGES IDENTIFIED FOR FINAN-**
14 **CIAL ACCOUNTING PURPOSES.**

15 (a) IN GENERAL.—Section 1221 is amended by add-
16 ing at the end the following new subsection:

17 “(c) HEDGING TRANSACTION.—For purposes of this
18 section—

19 “(1) IN GENERAL.—The term ‘hedging trans-
20 action’ means any transaction described in para-
21 graph (2) and identified under paragraph (3).

22 “(2) TRANSACTION DESCRIBED.—A transaction
23 is described in this paragraph if such transaction is
24 entered into by the taxpayer in the normal course of
25 the taxpayer’s trade or business primarily—

1 “(A) to manage risk of price changes or
2 currency fluctuations with respect to ordinary
3 property which is held or to be held by the tax-
4 payer,

5 “(B) to manage risk of interest rate or
6 price changes or currency fluctuations with re-
7 spect to borrowings made or to be made, or or-
8 dinary obligations incurred or to be incurred, by
9 the taxpayer, or

10 “(C) to manage such other risks as the
11 Secretary may prescribe in regulations.

12 “(3) IDENTIFICATION.—A transaction is identi-
13 fied under this paragraph if—

14 “(A) such transaction is clearly identified
15 as a hedging transaction for purposes of this
16 paragraph before the close of the day on which
17 it was acquired, originated, or entered into (or
18 such other time as the Secretary may by regula-
19 tions prescribe), or

20 “(B) such transaction is treated as a hedg-
21 ing transaction (within the meaning of generally
22 accepted accounting principles) for purposes of
23 an audited financial statement of the taxpayer
24 which—

1 “(i) is certified as being prepared in
2 accordance with generally accepted ac-
3 counting principles, and

4 “(ii) is used for the purposes of a
5 statement or report—

6 “(I) to shareholders, partners, or
7 other proprietors, or to beneficiaries,
8 or

9 “(II) for credit purposes.

10 “(4) TREATMENT OF NONIDENTIFICATION OR
11 IMPROPER IDENTIFICATION OF HEDGING TRANS-
12 ACTIONS.—The Secretary shall prescribe regulations
13 to properly characterize any income, gain, expense,
14 or loss arising from a transaction—

15 “(A) which would be a hedging transaction
16 if identified under paragraph (3), or

17 “(B) which is identified under paragraph
18 (3) but is not a transaction described in para-
19 graph (2).

20 In the case of a transaction identified under para-
21 graph (3) solely by reason of paragraph (3)(B), sub-
22 paragraph (B) of this paragraph shall not apply
23 with respect to such transaction unless the taxpayer
24 treats such transaction as a hedging transaction for
25 purposes of any provision of this title.”.

1 (b) CONFORMING AMENDMENTS.—

2 (1) Section 856(c)(5)(G)(i) is amended by strik-
3 ing “(as defined in clause (ii) or (iii) of section
4 1221(b)(2)(A)) which is clearly identified pursuant
5 to section 1221(a)(7)” and inserting “(as defined in
6 section 1221(c) (determined without regard to para-
7 graph (2)(A) thereof)”.

8 (2) Section 954(c)(5)(A) is amended by striking
9 “if such transaction—” and all that follows and in-
10 sserting the following: “if such transaction is a hedg-
11 ing transaction (as defined in section 1221(c)), de-
12 termined—

13 “(i) without regard to paragraph
14 (1)(B) thereof,

15 “(ii) by applying paragraph (1)(A)
16 thereof by substituting ‘ordinary property
17 or property described in section 1231(b)’
18 for ‘ordinary property’, and

19 “(iii) by substituting ‘controlled for-
20 eign corporation’ for ‘taxpayer’ each place
21 it appears.”.

22 (3) Section 1221(a)(7) is amended by striking
23 “which is clearly” and all that follows through “reg-
24 ulations prescribe)”.

1 (4)(A) Section 1221(b), as amended by this
2 Act, is amended by striking paragraph (2) and by
3 redesignating paragraphs (3) and (4) as paragraphs
4 (1) and (2), respectively.

5 (B) Section 170(e)(1)(A) is amended by strik-
6 ing “section 1221(b)(3)” and inserting “section
7 1221(b)(1)”.

8 (c) EFFECTIVE DATE.—The amendments made by
9 this section shall apply to transactions entered into after
10 December 31, 2013.

11 **PART 2—TREATMENT OF DISCOUNT AND**
12 **PREMIUM**

13 **SEC. 411. DETERMINATION OF ISSUE PRICE IN THE CASE**
14 **OF SPECIFIED DEBT MODIFICATIONS.**

15 (a) IN GENERAL.—Subpart A of part V of sub-
16 chapter P is amended by inserting after section 1274A
17 the following new section:

18 **“SEC. 1274B. DETERMINATION OF ISSUE PRICE IN THE**
19 **CASE OF SPECIFIED DEBT MODIFICATIONS.**

20 “(a) IN GENERAL.—In the case of any specified debt
21 modification, for purposes of this subpart, the issue price
22 of the modified debt instrument (whether by exchange or
23 significant modification) shall be the lesser of—

24 “(1) the adjusted issue price of the existing
25 debt instrument, or

1 “(2) the issue price of such modified debt in-
2 strument which would be determined under section
3 1274 if such modified debt instrument were a debt
4 instrument to which such section applied.

5 “(b) ADJUSTED ISSUE PRICE.—

6 “(1) IN GENERAL.—For purposes of subsection
7 (a)(1), the adjusted issue price of the existing debt
8 instrument is its issue price, increased by the por-
9 tion of any original issue discount previously includ-
10 ible in the gross income of any holder (without re-
11 gard to subsection (a)(7) or (b)(4) of section 1272
12 (or the corresponding provisions of prior law)).

13 “(2) SPECIAL RULE FOR APPLYING SECTION
14 163(e).—For purposes of section 163(e), the ad-
15 justed issue price of the existing debt instrument is
16 its issue price, increased by any original issue dis-
17 count previously allowed as a deduction.

18 “(c) SPECIFIED DEBT MODIFICATION.—For pur-
19 poses of this section, the term ‘specified debt modification’
20 means—

21 “(1) the exchange by an issuer of a new debt
22 instrument for an existing debt instrument issued by
23 such issuer, and

24 “(2) the significant modification of an existing
25 debt instrument, including a significant modification

1 of an existing debt instrument which is accomplished
2 by the issuer and holder indirectly through one or
3 more transactions with unrelated parties.”.

4 (b) CONFORMING AMENDMENTS.—

5 (1) Section 108(e)(10)(B) is amended by strik-
6 ing “and 1274” and inserting “, 1274, and 1274B”.

7 (2) Section 1274(c)(3) is amended by adding at
8 the end the following new subparagraph:

9 “(G) CERTAIN MODIFIED DEBT.—Any debt
10 instrument the issue price of which is deter-
11 mined under section 1274B.”.

12 (3) The table of sections for subpart A of part
13 V of subchapter P is amended by inserting after the
14 item relating to section 1274A the following new
15 item:

“Sec. 1274B. Determination of issue price in the case of specified debt modi-
fications.”.

16 (c) EFFECTIVE DATE.—The amendments made by
17 this section shall apply to transactions after December 31,
18 2013.

19 **SEC. 412. DEDUCTION FOR AMORTIZABLE BOND PREMIUM**
20 **ALLOWED IN DETERMINING ADJUSTED**
21 **GROSS INCOME.**

22 (a) IN GENERAL.—Subsection (a) of section 62 is
23 amended by inserting after paragraph (7) the following
24 new paragraph:

1 “(8) AMORTIZABLE BOND PREMIUM.—The de-
2 duction allowed under section 171(a)(1).”.

3 (b) EFFECTIVE DATE.—The amendments made by
4 this section shall apply to taxable years beginning after
5 December 31, 2013.

6 **SEC. 413. CURRENT INCLUSION IN INCOME OF MARKET**
7 **DISCOUNT.**

8 (a) IN GENERAL.—Subpart B of part V of sub-
9 chapter P of chapter 1 is amended by redesignating sec-
10 tion 1278 as section 1279 and by inserting after section
11 1277 the following new section:

12 **“SEC. 1278. CURRENT INCLUSION IN INCOME OF MARKET**
13 **DISCOUNT ON BONDS ACQUIRED AFTER 2013.**

14 “(a) IN GENERAL.—There shall be included in the
15 gross income of the holder of any market discount bond
16 acquired after December 31, 2013, an amount equal to
17 the sum of the daily portions of the market discount for
18 each day during the taxable year on which such holder
19 held such bond.

20 “(b) DETERMINATION OF DAILY PORTIONS.—

21 “(1) IN GENERAL.—For purposes of subsection
22 (a), the daily portion of the market discount on any
23 market discount bond shall be the daily portion
24 which would be determined under section 1272(a)(3)
25 if such bond had been—

1 “(A) originally issued on the date on which
2 such bond was acquired by the taxpayer,

3 “(B) for an issue price equal to the basis
4 of such bond immediately after such acqui-
5 sition.

6 “(2) LIMITATION ON DAILY PORTION.—The
7 daily portion determined under paragraph (1) shall
8 not exceed the amount that would be so determined
9 if the amount under subparagraph (B) thereof was
10 the imputed principal amount determined under sec-
11 tion 1274(b) by using a discount rate equal to the
12 greater of—

13 “(A) such bonds’s yield to maturity (deter-
14 mined as of the date of the issuance of such
15 bond) plus 5 percentage points, or

16 “(B) the applicable Federal rate for such
17 bond (determined under section 1274(d) as of
18 the date of the acquisition of such bond) plus
19 10 percentage points.

20 “(3) REDUCTION FOR ORIGINAL ISSUE DIS-
21 COUNT.—Each daily portion determined under para-
22 graph (1) (after the application of paragraph (2))
23 shall be reduced by the daily portion of the original
24 issue discount determined under section 1272(a)
25 with respect to such bond for the day involved (or,

1 in the case of any bond to which section 1272(a)
2 does not apply, the daily portion of the original issue
3 discount which would be so determined if section
4 1272(a) applied to such bond).

5 “(c) SPECIAL RULES.—

6 “(1) ACCRUALS TREATED AS INTEREST.—Ex-
7 cept for purposes of sections 103, 871(a), 881,
8 1441, 1442, and 6049 (and such other provisions as
9 may be specified in regulations), any amount in-
10 cluded in gross income under this section shall be
11 treated as interest for purposes of this title.

12 “(2) BASIS ADJUSTMENT.—The basis of any
13 market discount bond in the hands of the taxpayer
14 shall be increased by the amount included in gross
15 income pursuant to this section.

16 “(d) EXCEPTION FOR CERTAIN DEBT INSTRUMENTS
17 SUBJECT TO RATABLE INCLUSION.—This section shall
18 not apply to any debt instrument to which section 1272(b)
19 applies.”.

20 (b) CURRENT INCLUSION OF MARKET DISCOUNT ON
21 SHORT-TERM NONGOVERNMENTAL BONDS.—Section
22 1283 is amended by striking subsection (c).

23 (c) COORDINATION WITH RULES RELATED TO
24 TREATING MARKET DISCOUNT AS ORDINARY INCOME
25 UPON DISPOSITION.—

1 (1) IN GENERAL.—Section 1276 is amended by
2 adding at the end the following new subsection:

3 “(e) COORDINATION WITH RULES FOR CURRENT IN-
4 CLUSION OF MARKET DISCOUNT.—This section shall not
5 apply to any market discount bond to which section 1278
6 applies.”.

7 (2) DEFERRAL OF INTEREST DEDUCTION.—
8 Section 1277 is amended by adding at the end the
9 following new subsection:

10 “(d) COORDINATION WITH RULES FOR CURRENT IN-
11 CLUSION OF MARKET DISCOUNT.—This section shall not
12 apply to any market discount bond to which section 1278
13 applies.”.

14 (3) ELECTION TO INCLUDE MARKET DISCOUNT
15 CURRENTLY.—Section 1279(b), as redesignated by
16 subsection (a), is amended by adding at the end the
17 following new paragraph:

18 “(5) COORDINATION WITH RULES FOR CUR-
19 RENT INCLUSION OF MARKET DISCOUNT.—This sub-
20 section shall not apply to any market discount bond
21 to which section 1278 applies.”.

22 (d) TREATMENT OF CERTAIN BONDS HELD BY
23 PARTNERSHIPS.—Section 1279(a), as redesignated by
24 subsection (a), is amended by adding at the end the fol-
25 lowing new paragraph:

1 “(6) TRANSFERS OF PARTNERSHIP INTER-
2 ESTS.—In the case of a transfer described in section
3 743 of an interest in a partnership holding a bond,
4 the partnership shall be treated as acquiring the
5 transferee partner’s proportionate share of such
6 bond at the time of such transfer.”.

7 (e) BROKER REPORTING OF INCLUDIBLE DISCOUNT
8 ON BONDS.—

9 (1) IN GENERAL.—Section 6045 is amended by
10 adding at the end the following new subsection:

11 “(i) DISCOUNT ON BONDS.—

12 “(1) IN GENERAL.—If any customer of a broker
13 holds a covered bond in an account with such broker
14 at any time during a calendar year—

15 “(A) such broker shall file a return under
16 subsection (a) for such calendar year, and

17 “(B) such return shall include with respect
18 to each such covered bond—

19 “(i) the amount (if any) includible in
20 the gross income of such customer as origi-
21 nal issue discount with respect to such
22 bond under section 1272 for periods dur-
23 ing such calendar year, and.

24 “(ii) the amount (if any) includible in
25 the gross income of such customer as mar-

1 ket discount with respect to such bond
2 under section 1278(a) for periods during
3 such calendar year.

4 “(2) COVERED BOND.—For purposes of this
5 subsection, the term ‘covered bond’ means any obli-
6 gation to which section 1272 or 1278(a) applies if
7 such obligation—

8 “(A) was acquired after December 31,
9 2013, through a transaction in the account in
10 which such obligation is held, or

11 “(B) was transferred to such account from
12 an account in which such obligation was a cov-
13 ered bond, but only if the broker received a
14 statement under section 6045A with respect to
15 the transfer.

16 “(3) STATEMENTS TO CUSTOMERS.—The re-
17 quirements of subsections (b) shall apply with re-
18 spect to any return filed under subsection (a) by
19 reason of this subsection.”.

20 (2) INFORMATION REQUIRED IN CONNECTION
21 WITH TRANSFERS OF COVERED BONDS TO BRO-
22 KERS.—Subsection (a) of section 6045A is amend-
23 ed—

1 (A) by inserting “or a covered bond (as de-
2 fined in section 6045(i)(2))” after “covered se-
3 curity (as defined in section 6045(g)(3))”, and

4 (B) by striking “section 6045(g)” and in-
5 serting “subsections (g) and (i) of section
6 6045”.

7 (3) COORDINATION WITH REPORTING BY
8 ISSUER OF ORIGINAL ISSUE DISCOUNT.—Paragraph
9 (6) of section 6049(d) is amended by adding at the
10 end the following new subparagraph:

11 “(C) PREVENTION OF DOUBLE REPORT-
12 ING.—Except as otherwise provided by the Sec-
13 retary, original issue discount with respect to
14 any obligation shall not be required to be re-
15 ported under this section if such original issue
16 discount is required to be reported with respect
17 to such obligation under section 6045(i).”.

18 (f) CONFORMING AMENDMENTS.—

19 (1) Section 751(e)(2) is amended by striking
20 “section 1278” in the matter following paragraph
21 (2) and inserting “section 1279”.

22 (2) Section 1042(d) is amended by striking
23 “section 1278(a)(2)(A)(ii)” in the matter following
24 paragraph (2) and inserting “section
25 1279(a)(2)(A)(ii)”.

1 (3) Section 1276 is amended by inserting “**ON**
2 **BONDS NOT SUBJECT TO CURRENT INCLU-**
3 **SION**” after “**ACCRUED MARKET DISCOUNT**” in
4 the heading thereof.

5 (4) Section 1277 is amended by inserting “**ON**
6 **BONDS NOT SUBJECT TO CURRENT INCLU-**
7 **SION**” after “**ACCRUED MARKET DISCOUNT**” in
8 the heading thereof.

9 (5) Section 1281 is amended by striking sub-
10 section (c).

11 (6) The table of sections for subpart B of part
12 V of subchapter P of chapter 1 is amended to read
13 as follows:

“Sec. 1276. Disposition gain representing accrued market discount on bonds
not subject to current inclusion treated as ordinary income.

“Sec. 1277. Deferral of interest deduction allocable to accrued market discount
on bonds not subject to current inclusion.

“Sec. 1278. Current inclusion in income of market discount on bonds acquired
after 2013.

“Sec. 1279. Definitions and special rules.”.

14 (g) **EFFECTIVE DATE.**—The amendments made by
15 this section shall apply to obligations acquired after De-
16 cember 31, 2013.

17 **SEC. 414. RULES REGARDING CERTAIN GOVERNMENT**
18 **DEBT.**

19 (a) **REPEAL OF CERTAIN SUPERCEDED RULES.**—

20 (1) **IN GENERAL.**—Subpart B of part II of sub-
21 chapter E of chapter 1 is amended by striking sec-

1 tion 454 (and by striking the item relating to such
2 section in the table of sections for such subpart).

3 (2) PRESERVATION OF RULES RELATED TO
4 UNITED STATES SAVINGS BONDS.—

5 (A) IN GENERAL.—Subpart A of part V of
6 subchapter P of chapter 1 is amended by in-
7 serting after section 1272 the following new
8 section:

9 **“SEC. 1272A. UNITED STATES SAVINGS BONDS.**

10 “(a) ELECTION TO INCLUDE INCREASE IN REDEMP-
11 TION PRICE IN INCOME.—A taxpayer holding a United
12 States savings bond may elect to treat any increase in the
13 redemption price as income received in the taxable year.
14 If any such election is made with respect to any such obli-
15 gation, it shall apply also to all such obligations owned
16 by the taxpayer at the beginning of the first taxable year
17 to which it applies and to all such obligations thereafter
18 acquired by the taxpayer and shall be binding for all sub-
19 sequent taxable years, unless on application by the tax-
20 payer the Secretary permits the taxpayer, subject to such
21 conditions as the Secretary deems necessary, to change to
22 a different method. In the case of any such obligations
23 owned by the taxpayer at the beginning of the first taxable
24 year to which his election applies, the increase in the re-
25 demption price of such obligations occurring between the

1 date of acquisition and the first day of such taxable year
2 shall also be treated as income received in such taxable
3 year.

4 “(b) TREATMENT UPON REDEMPTION OR FINAL MA-
5 TURITY.—The increase in redemption value of a United
6 States savings bond (to the extent not previously included
7 in gross income) in excess of the adjusted basis of such
8 bond shall be included in gross income in the earlier of
9 the taxable year in which the bond is redeemed or in the
10 taxable year of final maturity.

11 “(c) CROSS REFERENCES.—

12 “(1) For treatment of United States savings
13 bonds redeemed to pay qualified higher education
14 expenses, see section 135.

15 “(2) For exception from current inclusion of
16 original issue discount, see section 1272(a)(2)(B).

17 “(3) For exception from market discount rules,
18 see section 1279(a)(1)(B)(iii).”

19 (B) CLERICAL AMENDMENT.—The table of
20 sections for subpart A of part V of subchapter
21 P of chapter 1 is amended by inserting after
22 the item relating to section 1272 the following
23 new item:

“Sec. 1272A. United States savings bonds.”

24 (3) CONFORMING AMENDMENTS.—

1 (A) Section 852(b)(2) is amended by strik-
2 ing subparagraph (F) and redesignating sub-
3 paragraph (G) as subparagraph (F).

4 (B) Section 1283(d)(3) is amended by
5 striking “Section 454(b) and paragraphs” and
6 inserting “Paragraphs”.

7 (C) Section 7871(a)(6) is amended by add-
8 ing “and” at the end of subparagraph (A) and
9 by striking subparagraph (C).

10 (4) EFFECTIVE DATE.—The amendments made
11 by this subsection shall take effect on the date of the
12 enactment of this Act.

13 (b) REPEAL OF SPECIAL RULE FOR EXCHANGES OF
14 UNITED STATES OBLIGATIONS.—

15 (1) IN GENERAL.—Part III of subchapter O of
16 chapter 1 is amended by striking section 1037 (and
17 by striking the item relating to such section in the
18 table of sections for such part).

19 (2) CONFORMING AMENDMENTS.—

20 (A) Subsections (b) and (c) of section
21 1031 are each amended by striking “of section
22 1036(a), or of section 1037(a)” and inserting
23 “or of section 1036(a)”.

24 (B) Section 1031(d) is amended by strik-
25 ing “section 1036(a), or section 1037(a)” both

1 places it appears and inserting “or section
2 1036(a)”.

3 (3) EFFECTIVE DATE.—The amendments made
4 by this subsection shall apply to exchanges after De-
5 cember 31, 2013.

6 **PART 3—CERTAIN RULES FOR DETERMINING**
7 **GAIN AND LOSS**

8 **SEC. 421. COST BASIS OF SPECIFIED SECURITIES DETER-**
9 **MINED IN ACCORDANCE WITH AVERAGE**
10 **BASIS METHOD.**

11 (a) IN GENERAL.—Subsection (d) of section 1012 is
12 amended to read as follows:

13 “(d) COST BASIS OF SPECIFIED SECURITIES DETER-
14 MINED IN ACCORDANCE WITH AVERAGE BASIS METH-
15 OD.—

16 “(1) IN GENERAL.—In the case of the sale, ex-
17 change, or other disposition of a specified security
18 on or after January 1, 2014, the cost of such secu-
19 rity shall be determined under this section in accord-
20 ance with the average basis method.

21 “(2) TRANSITIONAL RULE FOR DETERMINING
22 AVERAGE BASIS.—Any specified security which is ac-
23 quired before January 1, 2014, shall be treated as
24 a separate account from any such security which is
25 acquired on or after such date.

1 “(3) SPECIAL RULE FOR CERTAIN SECURI-
2 TIES.—In the case of any specified security with re-
3 spect to which the applicable date is after January
4 1, 2014, this subsection shall be applied by sub-
5 stituting ‘the applicable date’ for ‘January 1, 2014’
6 each place it appears.”.

7 (b) CONFORMING AMENDMENTS.—

8 (1) Section 1012(c)(1) is amended by striking
9 “the conventions prescribed by regulations under
10 this section” and inserting “the method applicable
11 for determining the cost of such security”.

12 (2) Section 1012(c)(2)(A) is amended by strik-
13 ing “section 1012” and inserting “this section (as in
14 effect prior to the enactment of the Tax Reform Act
15 of 2013)”.

16 (3) Section 6045(g)(2)(B)(i) is amended by
17 striking “shall be determined—” and all that follows
18 and inserting “shall be determined in accordance
19 with the average basis method.”.

20 (c) EFFECTIVE DATE.—The amendments made by
21 this section shall apply to sales, exchanges, and other dis-
22 positions after December 31, 2013.

23 **SEC. 422. WASH SALES BY RELATED PARTIES.**

24 (a) APPLICATION OF WASH SALE RULES TO RE-
25 LATED PARTIES.—Subsection (a) of section 1091 is

1 amended by striking “the taxpayer has acquired” and in-
2 serting “the taxpayer (or a related party) has acquired”.

3 (b) DISALLOWANCE OF LOSS FROM WASH SALES IN-
4 VOLVING RELATED PARTIES.—Subsection (d) of section
5 1091 is amended by adding at the end the following: “The
6 preceding sentence shall not apply with respect to any ac-
7 quisition by a related party (other than the taxpayer’s
8 spouse).”

9 (c) RELATED PARTY.—Section 1091 is amended by
10 adding at the end the following new subsection:

11 “(g) RELATED PARTY.—For purposes of this sec-
12 tion—

13 “(1) IN GENERAL.—The term ‘related party’
14 means—

15 “(A) the taxpayer’s spouse,

16 “(B) any dependent of the taxpayer and
17 any other taxpayer with respect to whom the
18 taxpayer is a dependent,

19 “(C) any individual, corporation, partner-
20 ship, trust, or estate which controls, or is con-
21 trolled by, (within the meaning of section
22 954(d)(3)) the taxpayer or any individual de-
23 scribed in subparagraph (A) or (B) with respect
24 to the taxpayer (or any combination thereof),

1 “(D) any individual retirement plan, Ar-
2 cher MSA (as defined in section 220(d)), or
3 health savings account (as defined in section
4 223(d)), of the taxpayer or of any individual de-
5 scribed in subparagraph (A) or (B) with respect
6 to the taxpayer,

7 “(E) any account under a qualified tuition
8 program described in section 529 or a Coverdell
9 education savings account (as defined in section
10 530(b)) if the taxpayer, or any individual de-
11 scribed in subparagraph (A) or (B) with respect
12 to the taxpayer, is the designated beneficiary of
13 such account or has the right to make any deci-
14 sion with respect to the investment of any
15 amount in such account, and

16 “(F) any account under—

17 “(i) a plan described in section
18 401(a),

19 “(ii) an annuity plan described in sec-
20 tion 403(a),

21 “(iii) an annuity contract described in
22 section 403(b), or

23 “(iv) an eligible deferred compensa-
24 tion plan described in section 457(b) and

1 maintained by an employer described in
2 section 457(e)(1)(A),
3 if the taxpayer or any individual described in
4 subparagraph (A) or (B) with respect to the
5 taxpayer has the right to make any decision
6 with respect to the investment of any amount in
7 such account .

8 “(2) RULES FOR DETERMINING STATUS.—

9 “(A) RELATIONSHIPS DETERMINED AT
10 TIME OF ACQUISITION.—Determinations under
11 paragraph (1) shall be made as of the time of
12 the purchase or exchange referred to in sub-
13 section (a) except that determinations under
14 subparagraphs (A) and (B) of paragraph (1)
15 shall be made for the taxable year which in-
16 cludes such purchase or exchange.

17 “(B) DETERMINATION OF MARITAL STA-
18 TUS.—

19 “(i) IN GENERAL.—Except as pro-
20 vided in clause (ii), marital status shall be
21 determined under section 7703.

22 “(ii) SPECIAL RULE FOR MARRIED IN-
23 DIVIDUALS FILING SEPARATELY AND LIV-
24 ING APART.—A husband and wife who—

1 “(I) file separate returns for any
2 taxable year, and

3 “(II) live apart at all times dur-
4 ing such taxable year,
5 shall not be treated as married individuals.

6 “(3) REGULATIONS.—The Secretary shall issue
7 such regulations or other guidance as may be nec-
8 essary to prevent the avoidance of the purposes of
9 this subsection, including regulations which treat
10 persons as related parties if such persons are formed
11 or availed of to avoid the purposes of this sub-
12 section.”.

13 (d) EFFECTIVE DATE.—The amendments made by
14 this section shall apply to sales and other dispositions
15 after December 31, 2013.

16 **Subtitle B—[Additional Reforms to**
17 **Be Provided]**