

117TH CONGRESS  
1ST SESSION

**S.** \_\_\_\_\_

To amend the Internal Revenue Code of 1986 to modernize the tax treatment of derivatives and their underlying investments, and for other purposes.

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IN THE SENATE OF THE UNITED STATES

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Mr. WYDEN introduced the following bill; which was read twice and referred to the Committee on \_\_\_\_\_

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**A BILL**

To amend the Internal Revenue Code of 1986 to modernize the tax treatment of derivatives and their underlying investments, 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 (a) SHORT TITLE.—This Act may be cited as the  
5 “Modernization of Derivatives Tax Act of 2021”.

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  
9 to, or repeal of, a section or other provision, the reference

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

3 **SEC. 2. MODERNIZATION OF TAX TREATMENT OF CERTAIN**  
4 **DERIVATIVES.**

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

7 **“PART IV—TAX TREATMENT OF DERIVATIVES**  
8 **AND SIMILAR CONTRACTS**

“SUBPART A. DERIVATIVES

“SUBPART B. SIMILAR CONTRACTS

9 **“Subpart A—Derivatives**

“Sec. 491. Rules for treatment of derivatives.

“Sec. 492. Investment hedging units.

“Sec. 493. Derivative defined.

10 **“SEC. 491. RULES FOR TREATMENT OF DERIVATIVES.**

11 “(a) IN GENERAL.—For purposes of this title, if  
12 there is a taxable event with respect to a derivative or an  
13 underlying investment—

14 “(1) notwithstanding any other provision of this  
15 title, except as provided in subsection (b)(3)(A) or  
16 section 1032, gain or loss shall be recognized and  
17 taken into account in the taxable year in which the  
18 taxable event occurs, and

19 “(2) proper adjustment shall be made in the  
20 amount of any subsequent gain or loss for gain or  
21 loss taken into account by reason of paragraph (1).

1       “(b) RULES RELATING TO GAIN OR LOSS.—Notwith-  
2 standing any other provision of this title—

3           “(1) CHARACTER AND SOURCE OF GAIN OR  
4 LOSS.—

5           “(A) CHARACTER.—Except as provided in  
6 paragraph (3)(A), any item of income, deduc-  
7 tion, gain, or loss taken into account under sub-  
8 section (a) with respect to a taxable event shall  
9 be treated as—

10                   “(i) ordinary income or loss, and

11                   “(ii) attributable to a trade or busi-  
12 ness of the taxpayer for purposes of sec-  
13 tions 62(a) and 172(d)(4).

14           “(B) SOURCE OF GAIN OR LOSS FROM DE-  
15 RIVATIVES.—In the case of a taxable event with  
16 respect to a derivative, any item of income, de-  
17 duction, gain, or loss taken into account under  
18 subsection (a) shall be treated as derived from  
19 sources within the country of residence, incor-  
20 poration, or organization of the taxpayer.

21           “(2) DETERMINATION OF AMOUNT.—

22           “(A) IN GENERAL.—The amount of gain  
23 or loss taken into account under subsection (a)  
24 with respect to a taxable event shall be—

1                   “(i) in the case of a taxable event in-  
2                   volving the termination or transfer of a de-  
3                   rivative or the sale or exchange of an un-  
4                   derlying investment, the amount of gain or  
5                   loss determined under this title with re-  
6                   spect to the taxable event, or

7                   “(ii) in the case of any other taxable  
8                   event, the amount of gain or loss which  
9                   would be determined under this title if, im-  
10                  mediately before the taxable event—

11                  “(I) in the case of a derivative,  
12                  the derivative were terminated or  
13                  transferred at its fair market value, or

14                  “(II) in the case of an underlying  
15                  investment, the investment were sold  
16                  or exchanged at its fair market value.

17                  “(B) RELIANCE ON VALUATION.—For pur-  
18                  poses of subparagraph (A), the taxpayer may  
19                  rely on a valuation which is—

20                  “(i) provided to the taxpayer by a  
21                  broker under section 6045(b), or

22                  “(ii) determined under an applicable  
23                  financial statement.

24                  “(3) SPECIAL RULES FOR TAXABLE EVENTS  
25                  WITH RESPECT TO INVESTMENT HEDGING UNITS.—

1           “(A) IN GENERAL.—In the case of a tax-  
2           able event described in subsection (c)(2) with  
3           respect to a derivative or underlying investment  
4           (other than a termination or transfer of the de-  
5           rivative or the sale or exchange of the under-  
6           lying investment)—

7                   “(i) notwithstanding subsection (a),  
8                   built-in loss (if any) with respect to the de-  
9                   rivative or underlying investment shall not  
10                  be recognized and shall not be taken into  
11                  account by reason of such taxable event,  
12                  and

13                   “(ii) notwithstanding paragraph (1),  
14                   built-in gain (if any) with respect to the  
15                   underlying investment shall be treated as  
16                   long-term or short-term capital gain if the  
17                   built-in gain would have been so treated if  
18                   the investment were sold or exchanged at  
19                   its fair market value immediately before  
20                   the time that the built-in gain is deter-  
21                   mined under subparagraph (D).

22                  “(B) IDENTIFICATION.—For purposes of  
23                  this paragraph, the determination of which por-  
24                  tions of an underlying investment have been  
25                  deemed sold or exchanged in a taxable event

1 shall be made in the same manner as if there  
2 had been an actual sale or exchange.

3 “(C) BUILT-IN LOSS.—For purposes of  
4 this section, the term ‘built-in loss’ means, with  
5 respect to any derivative or underlying invest-  
6 ment in an investment hedging unit, any loss  
7 which would have been recognized and taken  
8 into account under subsection (a) if the deriva-  
9 tive were terminated or transferred, or the un-  
10 derlying investment were sold or exchanged, at  
11 its fair market value as of the later of the time  
12 that the investment hedging unit was estab-  
13 lished or the time that the derivative or the un-  
14 derlying investment became part of the invest-  
15 ment hedging unit.

16 “(D) BUILT-IN GAIN.—For purposes of  
17 this section, the term ‘built-in gain’ means, with  
18 respect to any underlying investment in an in-  
19 vestment hedging unit, any gain which would  
20 have been recognized and taken into account  
21 under subsection (a) if the underlying invest-  
22 ment were sold or exchanged at its fair market  
23 value as of the later of the time that the invest-  
24 ment hedging unit was established or the time

1           that the underlying investment became part of  
2           the investment hedging unit.

3           “(c) TAXABLE EVENT.—For purposes of this part,  
4 the term ‘taxable event’ means—

5           “(1) with respect to any derivative which is not  
6 part of an investment hedging unit—

7           “(A) the termination or transfer of such  
8 derivative, and

9           “(B) the close of any taxable year if the  
10 taxpayer has rights or obligations with respect  
11 to such derivative at such time, and

12           “(2) with respect to all derivatives and under-  
13 lying investments which are part of the same invest-  
14 ment hedging unit—

15           “(A) the establishment of the investment  
16 hedging unit,

17           “(B) the termination or transfer of any  
18 such derivative,

19           “(C) the sale or exchange of all or any por-  
20 tion of any such underlying investment,

21           “(D) the entering into of another deriva-  
22 tive, or the acquisition of an additional amount  
23 of such underlying investment, after the estab-  
24 lishment of the investment hedging unit if such  
25 derivative or additional amount is treated as

1 part of the investment hedging unit under sec-  
2 tion 492, and

3 “(E) in the case of—

4 “(i) an investment hedging unit with  
5 respect to which an election is in effect  
6 under section 492(b), the close of each  
7 business day, and

8 “(ii) any other investment hedging  
9 unit, the close of any taxable year if the  
10 applicable hedging period with respect to  
11 such unit includes such close.

12 “(3) TERMINATION OR TRANSFER.—For pur-  
13 poses of this part, the term ‘termination or transfer’  
14 includes, with respect to any derivative, any termi-  
15 nation or transfer by offsetting, by taking or making  
16 delivery, by exercise or being exercised, by assign-  
17 ment or being assigned, by lapse, by sale or other  
18 disposition, by assumption, or otherwise.

19 “(d) TREATMENT OF PAYMENTS WITH RESPECT TO  
20 CERTAIN DERIVATIVES.—Notwithstanding any other pro-  
21 vision of this title—

22 “(1) IN GENERAL.—Except as provided by the  
23 Secretary, in the case of a payment pursuant to a  
24 derivative (other than an option)—



1           “(A) any item of income, deduction, gain,  
2           or loss with respect to the payment shall be  
3           taken into account for purposes of this title at  
4           the time of the payment, and

5           “(B) proper adjustment shall be made in  
6           the amount of any subsequent gain or loss for  
7           items taken into account by reason of subpara-  
8           graph (A).

9           This paragraph shall not apply to a payment in con-  
10          nection with a taxable event.

11          “(2) RULES RELATING TO CHARACTER AND  
12          SOURCE OF GAIN OR LOSS.—In the case of any item  
13          of income, deduction, gain, or loss with respect to  
14          payments described in paragraph (1)—

15                 “(A) the rules of subsection (b)(1)(A) shall  
16                 apply in determining the character of such  
17                 item, and

18                 “(B) except as provided in section 871(m),  
19                 the rule of subsection (b)(1)(B) shall apply in  
20                 determining the source of such item.

21          “(e) SUSPENSION OF HOLDING PERIOD WHILE UN-  
22          DERLYING INVESTMENT PART OF INVESTMENT HEDGING  
23          UNIT.—For purposes of section 1222, in the case of any  
24          underlying investment which is part of an investment  
25          hedging unit, the holding period for such investment shall

1 not include any period during which the underlying invest-  
2 ment is part of such unit.

3 “(f) APPLICABLE FINANCIAL STATEMENT.—For  
4 purposes of this part, the term ‘applicable financial state-  
5 ment’ means—

6 “(1) a financial statement which is certified as  
7 being prepared in accordance with generally accept-  
8 ed accounting principles and which is—

9 “(A) a 10-K (or successor form), or an-  
10 nual statement to shareholders, required to be  
11 filed by the taxpayer with the United States Se-  
12 curities and Exchange Commission,

13 “(B) an audited financial statement of the  
14 taxpayer which is used for—

15 “(i) credit purposes,

16 “(ii) reporting to shareholders, part-  
17 ners, or other proprietors, or to bene-  
18 ficiaries, or

19 “(iii) any other substantial nontax  
20 purpose,

21 but only if there is no statement of the taxpayer  
22 described in subparagraph (A), or

23 “(C) filed by the taxpayer with any other  
24 Federal agency for purposes other than Federal  
25 tax purposes, but only if there is no statement

1 of the taxpayer described in subparagraph (A)  
2 or (B),

3 “(2) a financial statement which is made on the  
4 basis of international financial reporting standards  
5 and is filed by the taxpayer with an agency of a for-  
6 eign government which is equivalent to the United  
7 States Securities and Exchange Commission and  
8 which has reporting standards not less stringent  
9 than the standards required by such Commission,  
10 but only if there is no statement of the taxpayer de-  
11 scribed in paragraph (1), or

12 “(3) a financial statement filed by the taxpayer  
13 with any other regulatory or governmental body  
14 specified by the Secretary, but only if there is no  
15 statement of the taxpayer described in paragraph  
16 (1) or (2).

17 **“SEC. 492. INVESTMENT HEDGING UNITS.**

18 “(a) INVESTMENT HEDGING UNIT.—For purposes of  
19 this part—

20 “(1) IN GENERAL.—Except as provided in sub-  
21 section (b)—

22 “(A) a taxpayer shall be treated as having  
23 an investment hedging unit with respect to an  
24 underlying investment during any applicable

1 hedging period with respect to the underlying  
2 investment, and

3 “(B) subject to paragraph (3), such invest-  
4 ment hedging unit shall at any time during the  
5 applicable hedging period consist of the fol-  
6 lowing held by the taxpayer at such time:

7 “(i) Each derivative with respect to  
8 the underlying investment which has a  
9 delta with respect to any portion of the un-  
10 derlying investment which is within the  
11 range beginning with minus 0.7 and end-  
12 ing with minus 1.0.

13 “(ii) Each portion of the underlying  
14 investment described in clause (i) with re-  
15 spect to which any derivative has a delta  
16 within the range described in clause (i).

17 “(2) APPLICABLE HEDGING PERIOD.—The term  
18 ‘applicable hedging period’ means, with respect to  
19 any underlying investment of a taxpayer, a contin-  
20 uous period—

21 “(A) beginning with the first time (after a  
22 period which is not an applicable hedging pe-  
23 riod) the taxpayer holds 1 or more of the de-  
24 rivatives with respect to the underlying invest-  
25 ment, and 1 or more portions of the underlying

1 investment, which are described in paragraph  
2 (1)(B), and

3 “(B) ending with the time none of such de-  
4 rivatives and portions are so described.

5 “(3) SPECIAL RULES RELATING TO DELTA AND  
6 COMBINING DERIVATIVES.—

7 “(A) IN GENERAL.—For purposes of this  
8 subsection—

9 “(i) a derivative with respect to an  
10 underlying investment shall be treated as  
11 having a delta within the range described  
12 in paragraph (1)(B)(i) if the derivative by  
13 itself, or in combination with 1 or more  
14 other derivatives, has such delta with re-  
15 spect to any portion of such underlying in-  
16 vestment, and

17 “(ii) the determination under para-  
18 graph (1)(B) of which derivatives have  
19 such delta, and each portion of the under-  
20 lying investment with respect to which  
21 such derivatives have such delta, shall be  
22 made in the manner which results in the  
23 largest portion of such underlying invest-  
24 ment being so described.

1           “(B) SECRETARIAL AUTHORITY FOR AP-  
2           PLICABLE TRADED DERIVATIVES.—The Sec-  
3           retary may prescribe regulations or other guid-  
4           ance to modify the rules under subparagraph  
5           (A) to simplify the application of such rules to  
6           applicable traded derivatives.

7           “(4) APPLICABLE TRADED DERIVATIVES.—For  
8           purposes of paragraph (3)—

9           “(A) IN GENERAL.—The term ‘applicable  
10           traded derivative’ means any listed option or  
11           regulated futures contract.

12           “(B) REGULATED FUTURES CONTRACT.—  
13           The term ‘regulated futures contract’ means a  
14           contract—

15           “(i) with respect to which the amount  
16           required to be deposited and the amount  
17           which may be withdrawn depends on a sys-  
18           tem of marking to market, and

19           “(ii) which is traded on (or subject to  
20           the rules of) a qualified board or exchange.

21           “(C) LISTED OPTION.—The term ‘listed  
22           option’ means any option (other than a right to  
23           acquire stock from the issuer) which is traded  
24           on (or subject to the rules of) a qualified board  
25           or exchange.

1 “(D) QUALIFIED BOARD OR EXCHANGE.—

2 The term ‘qualified board or exchange’  
3 means—

4 “(i) a national securities exchange  
5 which is registered with the Securities and  
6 Exchange Commission,

7 “(ii) a domestic board of trade des-  
8 ignated as a contract market by the Com-  
9 modity Futures Trading Commission, or

10 “(iii) any other exchange, board of  
11 trade, or other market which the Secretary  
12 determines has rules adequate to carry out  
13 the purposes of this part.

14 “(b) ELECTION WITH RESPECT TO ITEMS INCLUDED  
15 IN INVESTMENT HEDGING UNIT.—

16 “(1) IN GENERAL.—For purposes of this part,  
17 a taxpayer may elect to treat all derivatives with re-  
18 spect to an underlying investment, and all of such  
19 underlying investment, as part of an investment  
20 hedging unit.

21 “(2) ELECTION.—Any election under this sub-  
22 section with respect to an underlying investment—

23 “(A) shall apply to all derivatives with re-  
24 spect to such underlying investment, and all of  
25 such underlying investment, held at any time

1 after the election is made (including during any  
2 period such derivatives or underlying invest-  
3 ment are not held simultaneously), and

4 “(B) shall be irrevocable.

5 “(3) DEEMED ELECTION FOR TAXPAYERS FAIL-  
6 ING TO IDENTIFY.—

7 “(A) IN GENERAL.—If a taxpayer—

8 “(i) does not have an election in effect  
9 under paragraph (1) with respect to an un-  
10 derlying investment, and

11 “(ii) fails to meet the requirements of  
12 subsection (c) for testing and identifying  
13 derivatives with respect to the underlying  
14 investment,

15 the taxpayer shall be treated as having made  
16 the election under paragraph (1).

17 “(B) TREATMENT OF ELECTION.—For  
18 purposes of paragraph (2), a deemed election  
19 under this paragraph—

20 “(i) shall be treated as made as of the  
21 first time the taxpayer fails to meet the re-  
22 quirements of subsection (c) with respect  
23 to the underlying investment, and



1                   “(ii) notwithstanding paragraph  
2                   (2)(B), may be revoked with the consent of  
3                   the Secretary.

4           “(c) DEFINITIONS AND RULES RELATING TO TAX-  
5 PAYERS IDENTIFYING INVESTMENT HEDGING UNITS.—In  
6 the case of a taxpayer with respect to which an election  
7 is not in effect under subsection (b) with respect to an  
8 underlying investment—

9           “(1) IN GENERAL.—The taxpayer shall, at the  
10           times described in paragraph (3), test the derivatives  
11           with respect to the underlying investment and make  
12           the identifications described in paragraph (2).

13           “(2) IDENTIFICATION.—

14           “(A) IN GENERAL.—The taxpayer shall  
15           identify the following with respect to an under-  
16           lying investment:

17                   “(i) Each derivative described in sub-  
18                   section (a)(1)(B)(i).

19                   “(ii) Each portion of the underlying  
20                   investment described in subsection  
21                   (a)(1)(B)(ii).

22           “(B) DERIVATIVES AND UNDERLYING IN-  
23 VESTMENT NOT PART OF INVESTMENT HEDG-  
24 ING UNIT.—A taxpayer shall identify the de-  
25 rivatives with respect to an underlying invest-

1           ment, and the portions of the underlying invest-  
2           ment, which are not required to be identified  
3           under subparagraph (A).

4           “(C) PORTION MAY INCLUDE ALL OF UN-  
5           DERLYING INVESTMENT.—For purposes of this  
6           part, the term ‘portion’ with respect to any un-  
7           derlying investment identified may include all of  
8           the underlying investment.

9           “(3) TIMES IDENTIFICATIONS REQUIRED TO BE  
10          MADE.—

11           “(A) IN GENERAL.—The taxpayer shall  
12           test and make the identifications required  
13           under this subsection at the following times  
14           during any continuous period the taxpayer si-  
15           multaneously holds 1 or more derivatives with  
16           respect to an underlying investment and 1 or  
17           more portions of the underlying investment:

18                   “(i) The beginning of the period.

19                   “(ii) Immediately after the taxpayer  
20           (during such period)—

21                   “(I) enters into another deriva-  
22           tive with respect to the underlying in-  
23           vestment or acquires an additional  
24           amount of such underlying invest-  
25           ment, or

1                   “(II) terminates or transfers 1 or  
2                   more derivatives with respect to the  
3                   underlying investment or sells or ex-  
4                   changes any portion of the underlying  
5                   investment, except that no testing and  
6                   identification shall be required under  
7                   this subclause with respect to any  
8                   such transaction if the taxpayer does  
9                   not have an investment hedging unit  
10                  with respect to the underlying invest-  
11                  ment immediately before such trans-  
12                  action.

13                  “(iii) Such other times during such  
14                  period as the Secretary may prescribe by  
15                  regulations or other guidance.

16                  “(B) NO OTHER TIMES FOR TESTING.—  
17                  Except as provided by the Secretary, there shall  
18                  not be taken into account for purposes of this  
19                  part any testing and identification done by the  
20                  taxpayer with respect to an underlying invest-  
21                  ment at a time other than the times required  
22                  under subparagraph (A).

23                  “(4) MANNER.—A taxpayer shall be treated as  
24                  timely making the identifications required under this  
25                  subsection if the derivatives with respect to, and

1 each portion of, an underlying investment are clearly  
2 identified as part of (or as not part of) the invest-  
3 ment hedging unit for purposes of this paragraph  
4 before the close of the day on which the identifica-  
5 tion is required (or such other time as the Secretary  
6 may prescribe).

7 “(5) TREATMENT OF INCORRECT IDENTIFICA-  
8 TION.—The Secretary shall prescribe regulations or  
9 other guidance to properly characterize any income,  
10 gain, expense, or loss arising from any derivative or  
11 underlying investment which is incorrectly identified  
12 under paragraph (2) as being part of, or not being  
13 part of, an investment hedging unit.

14 “(d) DELTA.—For purposes of this section—

15 “(1) IN GENERAL.—The term ‘delta’ means,  
16 with respect to any derivative and underlying invest-  
17 ment, the ratio of the expected change in the fair  
18 market value of the derivative to a very small change  
19 in the fair market value of the underlying invest-  
20 ment.

21 “(2) METHOD OF DETERMINATION.—The delta  
22 with respect to any derivative with respect to an un-  
23 derlying investment (or any combination of such de-  
24 rivatives) shall be determined—

1           “(A) in a commercially reasonable manner,  
2           and

3           “(B) except as provided by the Secretary,  
4           in a manner which is consistent with the man-  
5           ner used by the taxpayer or the taxpayer’s  
6           broker for purposes of an applicable financial  
7           statement.

8           “(3) TIME FOR MAKING DETERMINATION.—The  
9           delta with respect to any derivative and underlying  
10          investment shall be determined as of any date the  
11          taxpayer is required to make the identifications de-  
12          scribed in subsection (c).

13          “(4) MULTIPLE UNDERLYING INVESTMENTS.—

14                 “(A) IN GENERAL.—Except as provided in  
15                 subparagraph (B), if the value of a derivative is  
16                 determined by reference to more than 1 under-  
17                 lying investment, the delta shall be determined  
18                 separately with respect to each underlying in-  
19                 vestment.

20                 “(B) METHODS FOR COMBINATIONS OF  
21                 UNDERLYING INVESTMENTS.—The Secretary  
22                 may provide methods for determining the delta  
23                 of any derivative with respect to combinations  
24                 of 2 or more underlying investments.

1           “(e) OTHER DEFINITIONS AND RULES.—For pur-  
2 poses of this part—

3           “(1) UNDERLYING INVESTMENT.—

4                   “(A) IN GENERAL.—The term ‘underlying  
5 investment’ means, with respect to any deriva-  
6 tive, any item—

7                           “(i) which is described in any of the  
8 paragraphs (1) through (8) of section  
9 493(a) (or any item substantially the same  
10 as any such item), and

11                           “(ii) by reference to which the value  
12 of the derivative, or any payment or other  
13 transfer with respect to the derivative, is  
14 determined either directly or indirectly.

15           “(B) COORDINATION WITH SECTION 475.—

16           In the case of a dealer in securities to which  
17 section 475 applies (and a dealer in commod-  
18 ities with respect to which an election is in ef-  
19 fect under section 475(e)), such term shall not  
20 include any item which, but for this subpara-  
21 graph, would be treated as an underlying in-  
22 vestment if such item is treated as a security  
23 under section 475 (including a commodity  
24 treated as a security under section 475(e)).

1           “(C) INDIRECT DETERMINATIONS.—For  
2 purposes of subparagraph (A)(ii), the value of,  
3 or any payment or other transfer with respect  
4 to, a derivative shall not be treated as indirectly  
5 determined by reference to one or more of the  
6 items described in paragraphs (1) through (8)  
7 of section 493(a) solely because the change in  
8 a variable affecting such value, payment, or  
9 other transfer also affects the value, level,  
10 amount, or calculation of such item or items.

11           “(2) ESTABLISHMENT OF INVESTMENT HEDG-  
12 ING UNIT.—A taxpayer shall be treated as having  
13 established an investment hedging unit with respect  
14 to an underlying investment—

15           “(A) in the case of a taxpayer with an  
16 election in effect under subsection (b) with re-  
17 spect to the underlying investment, as of the  
18 date the election takes effect, and

19           “(B) in the case of any other taxpayer, as  
20 of the beginning of each applicable hedging pe-  
21 riod with respect to the underlying investment.

22           “(3) RELATED PARTIES, ETC.—For purposes of  
23 this section—

24           “(A) ATTRIBUTION BETWEEN RELATED  
25 PERSONS.—Any derivative or underlying invest-

1           ment held by a related party (within the mean-  
2           ing of subsection (f)) with respect to the tax-  
3           payer shall be treated as held by the taxpayer.

4           “(B) CERTAIN PASS-THROUGH ENTI-  
5           TIES.—If part or all of the income, gain, loss,  
6           or expense with respect to a derivative or un-  
7           derlying investment held by a partnership,  
8           trust, or other entity would properly be taken  
9           into account for purposes of this chapter by the  
10          taxpayer, then, except to the extent otherwise  
11          provided by the Secretary, such derivative or in-  
12          vestment shall be treated as held by the tax-  
13          payer.

14          “(C) STOCK AND DEBT WHOSE VALUE PRI-  
15          MARILY DETERMINED BY REFERENCE TO  
16          OTHER ITEMS.—Except as provided by the Sec-  
17          retary, if the taxpayer holds an item described  
18          in paragraph (1) or (3) of section 493(a) the  
19          value of which, or with respect to which any  
20          payment or other transfer, is primarily deter-  
21          mined by reference to one or more other items  
22          described in paragraphs (1) through (8) of sec-  
23          tion 493(a), then, solely for purposes of this  
24          subpart, such item described in paragraph (1)



1           or (3) of section 493(a) shall also be treated as  
2           if it were such other item.

3           “(f) RELATED PARTY.—For purposes of this sec-  
4 tion—

5           “(1) IN GENERAL.—A person is a related party  
6           to the taxpayer if, with respect to any period during  
7           which a derivative or underlying investment is held  
8           by such person, such person—

9                   “(A) is the taxpayer’s spouse,

10                   “(B) is a dependent of the taxpayer or any  
11           other taxpayer with respect to whom the tax-  
12           payer is a dependent,

13                   “(C) is an individual, corporation, partner-  
14           ship, trust, or estate which controls, or is con-  
15           trolled by (within the meaning of section  
16           954(d)(3)), the taxpayer or any individual de-  
17           scribed in subparagraph (A) or (B) with respect  
18           to the taxpayer (or any combination thereof),

19                   “(D) is an individual retirement plan, Ar-  
20           cher MSA (as defined in section 220(d)), or  
21           health savings account (as defined in section  
22           223(d)), of the taxpayer or of any individual de-  
23           scribed in subparagraph (A) or (B) with respect  
24           to the taxpayer,

1           “(E) is an account under a qualified tui-  
2           tion program described in section 529, an  
3           ABLE account (as defined in section  
4           529A(e)(6)), or a Coverdell education savings  
5           account (as defined in section 530(b)) if the  
6           taxpayer, or any individual described in sub-  
7           paragraph (A) or (B) with respect to the tax-  
8           payer, is the designated beneficiary of such ac-  
9           count or has the right to make any decision  
10          with respect to the investment of any amount in  
11          such account,

12           “(F) is an account under—

13           “(i) a plan described in section  
14           401(a),

15           “(ii) an annuity plan described in sec-  
16           tion 403(a),

17           “(iii) an annuity contract described in  
18           section 403(b), or

19           “(iv) an eligible deferred compensa-  
20           tion plan described in section 457(b) and  
21           maintained by an employer described in  
22           section 457(e)(1)(A),

23          if the taxpayer or any individual described in  
24          subparagraph (A) or (B) with respect to the  
25          taxpayer has the right to make any decision

1 with respect to the investment of any amount in  
2 such account, or

3 “(G) files a consolidated return (within the  
4 meaning of section 1501) with the taxpayer for  
5 any taxable year which includes a portion of  
6 such period.

7 “(2) DETERMINATION OF MARITAL STATUS.—

8 “(A) IN GENERAL.—Except as provided in  
9 subparagraph (B), marital status shall be deter-  
10 mined under section 7703.

11 “(B) SPECIAL RULE FOR MARRIED INDI-  
12 VIDUALS FILING SEPARATELY AND LIVING  
13 APART.—A husband and wife who—

14 “(i) file separate returns for any tax-  
15 able year, and

16 “(ii) live apart at all times during  
17 such taxable year,

18 shall not be treated as married individuals.

19 “(g) REGULATIONS.—The Secretary shall prescribe  
20 such regulations or other guidance as may be appropriate  
21 to carry out this section, including regulations or guidance  
22 which require in appropriate cases a taxpayer to bifurcate  
23 derivatives described in subsection (d)(4) for purposes of  
24 applying this part or which may be necessary to prevent  
25 the avoidance of the purposes of subsection (f) (including

1 treating persons as related parties if such persons are  
2 formed or availed of to avoid the purposes of such sub-  
3 section).

4 **“SEC. 493. DERIVATIVE DEFINED.**

5 “(a) IN GENERAL.—For purposes of this part, except  
6 as otherwise provided in this section, the term ‘derivative’  
7 means any contract (including any option, forward con-  
8 tract, futures contract, short position, swap, or similar  
9 contract) the value of which, or any payment or other  
10 transfer with respect to which, is (directly or indirectly)  
11 determined by reference to one or more of the following:

12 “(1) Any share of stock in a corporation.

13 “(2) Any partnership or beneficial ownership  
14 interest in a partnership or trust.

15 “(3) Any evidence of indebtedness.

16 “(4) Except as provided in subsection (b)(1),  
17 any real property.

18 “(5) Any commodity which is actively traded  
19 (within the meaning of section 1092(c)(4)).

20 “(6) Any currency.

21 “(7) Any rate, price, amount, index, formula, or  
22 algorithm.

23 “(8) Any other item which the Secretary may  
24 prescribe.

1 Except as provided by the Secretary to prevent the avoid-  
2 ance of the purposes of this part, such term shall not in-  
3 clude any item described in paragraphs (1) through (8).  
4 For purposes of this subsection, the value of, or any pay-  
5 ment or other transfer with respect to, a contract shall  
6 not be treated as indirectly determined by reference to one  
7 or more of the items described in paragraphs (1) through  
8 (8) solely because the change in a variable affecting such  
9 value, payment, or other transfer also affects the value,  
10 level, amount, or calculation of such item or items.

11 “(b) EXCEPTIONS.—

12 “(1) CERTAIN REAL PROPERTY.—

13 “(A) IN GENERAL.—For purposes of this  
14 part, the term ‘derivative’ shall not include any  
15 contract with respect to interests in real prop-  
16 erty (as defined in section 856(c)(5)(C)) if such  
17 contract requires physical delivery of such real  
18 property.

19 “(B) OPTIONS TO SETTLE IN CASH.—

20 “(i) IN GENERAL.—For purposes of  
21 subparagraph (A), a contract which pro-  
22 vides for an option of cash settlement shall  
23 not be treated as requiring physical deliv-  
24 ery of real property unless the option is ex-

1 exercisable only in unusual and exceptional  
2 circumstances.

3 “(ii) OPTION OF CASH SETTLE-  
4 MENT.—For purposes of clause (i), a con-  
5 tract provides an option of cash settlement  
6 if the contract settles in (or could be set-  
7 tled in) cash or property other than the  
8 underlying real property.

9 “(2) HEDGING TRANSACTIONS.—

10 “(A) IN GENERAL.—For purposes of this  
11 part, the term ‘derivative’ shall not include any  
12 contract which is part of a hedging transaction  
13 (as defined in section 1221(b)).

14 “(B) SECTION 988 HEDGING TRANS-  
15 ACTIONS.—For exception for section 988 hedg-  
16 ing transactions, see section 988(d)(1).

17 “(3) SECURITIES LENDING, SALE-REPURCHASE,  
18 AND SIMILAR FINANCING TRANSACTIONS.—To the  
19 extent provided by the Secretary, for purposes of  
20 this part, the term ‘derivative’ shall not include the  
21 right to the return of the same or substantially iden-  
22 tical securities transferred in a securities lending  
23 transaction, sale-repurchase transaction, or similar  
24 financing transaction.

1           “(4) OPTIONS RECEIVED IN CONNECTION WITH  
2           THE PERFORMANCE OF SERVICES.—For purposes of  
3           this part, the term ‘derivative’ shall not include any  
4           option described in section 83(e)(3) received in con-  
5           nection with the performance of services.

6           “(5) INSURANCE, ANNUITY, AND ENDOWMENT  
7           CONTRACTS.—For purposes of this part, the term  
8           ‘derivative’ shall not include any insurance, annuity,  
9           or endowment contract issued by an insurance com-  
10          pany to which subchapter L applies (or issued by  
11          any foreign corporation to which such subchapter  
12          would apply if such foreign corporation were a do-  
13          mestic corporation).

14          “(6) DERIVATIVES WITH RESPECT TO STOCK  
15          OF MEMBERS OF SAME WORLDWIDE AFFILIATED  
16          GROUP.—

17                 “(A) IN GENERAL.—For purposes of this  
18                 part, the term ‘derivative’ shall not include any  
19                 derivative (determined without regard to this  
20                 paragraph) with respect to stock issued by any  
21                 member of the same worldwide affiliated group  
22                 in which the taxpayer is a member.

23                 “(B) WORLDWIDE AFFILIATED GROUP.—  
24                 For purposes of this paragraph, the term

1           ‘worldwide affiliated group’ means a group con-  
2           sisting of—

3                   “(i) the includible members of an af-  
4                   filiated group (as defined in section  
5                   1504(a), determined without regard to  
6                   paragraph (2) of section 1504(b)), and

7                   “(ii) all controlled foreign corpora-  
8                   tions in which such members in the aggre-  
9                   gate meet the ownership requirements of  
10                  section 1504(a)(2) either directly or indi-  
11                  rectly through applying paragraph (2) of  
12                  section 958(a) or through applying rules  
13                  similar to the rules of such paragraph to  
14                  stock owned directly or indirectly by do-  
15                  mestic partnerships, trusts, or estates.

16                  “(7) COMMODITIES USED IN NORMAL COURSE  
17                  OF TRADE OR BUSINESS.—For purposes of this part,  
18                  the term ‘derivative’ shall not include any contract  
19                  with respect to any commodity if—

20                   “(A) such contract requires physical deliv-  
21                   ery with the option of cash settlement only in  
22                   unusual and exceptional circumstances, and

23                   “(B) such commodity is used (and is used  
24                   in quantities with respect to which such deriva-  
25                   tive relates) in the normal course of the tax-



1 payer's trade or business (or, in the case of an  
2 individual, for personal consumption).

3 “(c) CONTRACTS WITH EMBEDDED DERIVATIVE  
4 COMPONENTS.—

5 “(1) IN GENERAL.—If a contract has derivative  
6 and nonderivative components, then each derivative  
7 component shall be treated as a derivative for pur-  
8 poses of this part. If the derivative component can-  
9 not be separately valued, then the entire contract  
10 shall be treated as a derivative for purposes of this  
11 part.

12 “(2) EXCEPTION FOR CERTAIN EMBEDDED DE-  
13 RIVATIVE COMPONENTS OF DEBT INSTRUMENTS.—A  
14 debt instrument shall not be treated as having a de-  
15 rivative component merely because—

16 “(A) such debt instrument is denominated  
17 in a nonfunctional currency (as defined in sec-  
18 tion 988(c)(1)(C)(ii)), or

19 “(B) payments with respect to such debt  
20 instrument are determined by reference to the  
21 value of a nonfunctional currency (as so de-  
22 fined).

23 “(d) TREATMENT OF AMERICAN DEPOSITORY RE-  
24 CEIPTS AND SIMILAR INSTRUMENTS.—Except as other-  
25 wise provided by the Secretary, for purposes of this part,

1 American depository receipts (and similar instruments)  
2 with respect to shares of stock in foreign corporations  
3 shall be treated as shares of stock in such foreign corpora-  
4 tions.

5 **“Subpart B—Similar Contracts**

“Sec. 494. Tax treatment of contracts similar to derivatives.

6 **“SEC. 494. TAX TREATMENT OF CONTRACTS SIMILAR TO**  
7 **DERIVATIVES.**

8 “(a) IN GENERAL.—For purposes of this title, if  
9 there is a taxable transaction with respect to any applica-  
10 ble property interest, then, notwithstanding any other pro-  
11 vision of this title other than section 1032, gain or loss  
12 attributable to the taxable transaction shall be considered  
13 gain or loss from the sale or exchange of property which  
14 has the same character as the property to which the appli-  
15 cable property interest relates has (or would have) in the  
16 hands of the taxpayer.

17 “(b) DEFINITIONS.—For purposes of this section—

18 “(1) APPLICABLE PROPERTY INTEREST.—The  
19 term ‘applicable property interest’ means any right  
20 or obligation with respect to property other than—

21 “(A) a derivative (as defined in section  
22 493), or

23 “(B) any position in applicable property to  
24 which section 1092 applies.

1           “(2) TAXABLE TRANSACTION.—The term ‘tax-  
2           able transaction’ means, with respect to any applica-  
3           ble property interest—

4                   “(A) any termination or transfer (as de-  
5                   fined in section 491(c)(3)) of such interest, or

6                   “(B) any payment in fulfillment or partial  
7                   fulfillment of such interest.”.

8   **SEC. 3. COORDINATION OF NEW RULES WITH EXISTING**  
9                   **RULES.**

10           (a) COORDINATION WITH RULES FOR DEALERS AND  
11   TRADERS.—

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

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

16                           (B) by striking subparagraphs (D) and (E)  
17                           and by redesignating subparagraph (F) as sub-  
18                           paragraph (D),

19                           (C) by striking “subparagraph (A), (B),  
20                           (C), (D), or (E)” in subparagraph (D)(i), as so  
21                           redesignated, and inserting “subparagraph (A),  
22                           (B), or (C)”, and

23                           (D) by amending the last sentence to read  
24                           as follows: “Such term shall not include any de-  
25                           rivative to which section 491(a) applies.”.

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

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

5                   (B) by striking subparagraphs (B) and (C)  
6           and by redesignating subparagraph (D) as sub-  
7           paragraph (B), and

8                   (C) by striking “subparagraph (A), (B) or  
9           (C)” in subparagraph (B)(i), as so redesign-  
10          ated, and inserting “subparagraph (A)”.

11          (3) CONFORMING AMENDMENTS.—

12                  (A) Section 475(b) is amended by striking  
13          paragraph (4).

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

15                          (i) by striking “subsection  
16                          (c)(2)(F)(iii)” and inserting “subsection  
17                          (c)(2)(D)(iii)”, and

18                          (ii) by striking “subsection (c)(2)(F)”  
19                          and inserting “subsection (c)(2)(D)”.

20                  (C) Section 475(f)(1)(D) is amended by  
21          striking “subsections (b)(4) and (d)” and in-  
22          serting “subsection (d)”.

23          (b) COORDINATION WITH STRADDLE RULES.—

24                  (1) IN GENERAL.—Section 1092 is amended to  
25          read as follows:

1 **“SEC. 1092. STRADDLES.**

2 “(a) RECOGNITION OF LOSS IN CASE OF STRAD-  
3 DLES, ETC.—

4 “(1) LIMITATION ON RECOGNITION OF LOSS.—

5 “(A) IN GENERAL.—Any loss with respect  
6 to 1 or more positions shall be taken into ac-  
7 count for any taxable year only to the extent  
8 that the amount of such loss exceeds the unrec-  
9 ognized gain (if any) with respect to 1 or more  
10 positions which were offsetting positions with  
11 respect to 1 or more positions from which the  
12 loss arose.

13 “(B) CARRYOVER OF LOSS.—Any loss  
14 which may not be taken into account under  
15 subparagraph (A) for any taxable year shall,  
16 subject to the limitations under subparagraph  
17 (A), be treated as sustained in the succeeding  
18 taxable year.

19 “(2) UNRECOGNIZED GAIN.—For purposes of  
20 this subsection—

21 “(A) IN GENERAL.—The term ‘unrecog-  
22 nized gain’ means—

23 “(i) in the case of any position held  
24 by the taxpayer as of the close of the tax-  
25 able year, the amount of gain which would  
26 be taken into account with respect to such

1 position if such position were sold on the  
2 last business day of such taxable year at  
3 its fair market value, and

4 “(ii) in the case of any position with  
5 respect to which, as of the close of the tax-  
6 able year, gain has been realized but not  
7 recognized, the amount of gain so realized.

8 “(B) REPORTING OF GAIN.—Each tax-  
9 payer shall disclose to the Secretary, at such  
10 time and in such manner and form as the Sec-  
11 retary may prescribe—

12 “(i) each position (whether or not  
13 part of a straddle) with respect to which,  
14 as of the close of the taxable year, there is  
15 unrecognized gain, and

16 “(ii) the amount of such unrecognized  
17 gain.

18 The Secretary may waive the requirement to re-  
19 port under this subparagraph with respect to  
20 any position if such reporting is not required to  
21 carry out the purposes of this section.

22 “(3) SPECIAL RULES FOR PHYSICALLY SET-  
23 TLED POSITIONS.—For purposes of this subsection,  
24 if a taxpayer settles a position which is part of a  
25 straddle by delivering property to which the position

1 relates (and such position, if terminated, would re-  
2 sult in a realization of a loss), then such taxpayer  
3 shall be treated as if such taxpayer—

4 “(A) terminated the position for its fair  
5 market value immediately before the settlement,  
6 and

7 “(B) sold the property so delivered by the  
8 taxpayer at its fair market value.

9 “(b) REGULATIONS.—The Secretary shall prescribe  
10 such regulations with respect to gain or loss on positions  
11 which are a part of a straddle as may be appropriate to  
12 carry out the purposes of this section and section 263(g).  
13 To the extent consistent with such purposes, such regula-  
14 tions shall include rules applying the principles of sub-  
15 sections (a) and (d) of section 1091 and of subsections  
16 (b) and (d) of section 1233 (as in effect before their re-  
17 peal).

18 “(c) DEFINITIONS AND RULES RELATING TO STRAD-  
19 DLES.—For purposes of this section—

20 “(1) STRADDLE DEFINED.—The term ‘straddle’  
21 means offsetting positions with respect to applicable  
22 property.

23 “(2) OFFSETTING POSITIONS.—A taxpayer  
24 holds offsetting positions with respect to applicable  
25 property if the taxpayer holds any position which by

1       itself, or in combination with 1 or more other posi-  
2       tions held by the taxpayer, has a delta (within the  
3       meaning of section 492(d)(1)) with respect to any  
4       other position held by the taxpayer which is within  
5       the range beginning with minus 0.7 and ending with  
6       minus 1.0. For purposes of this paragraph, positions  
7       shall be taken into account whether or not they are  
8       in the same applicable property.

9               “(3) DETERMINATION OF DELTA.—For pur-  
10       poses of this section—

11               “(A) METHOD OF DETERMINATION.—The  
12       delta with respect to any position in applicable  
13       property with respect to another position in ap-  
14       plicable property (or any combination of such  
15       positions) shall be determined in the same man-  
16       ner as under section 492(d)(2).

17               “(B) TIMING OF DELTA DETERMINATION  
18       AND OTHER SPECIAL RULES.—Rules similar to  
19       the rules of paragraphs (3) and (4) of section  
20       492(d) shall apply for purposes of this para-  
21       graph.

22               “(4) APPLICABLE PROPERTY AND POSITION DE-  
23       FINED.—

24               “(A) APPLICABLE PROPERTY.—The term  
25       ‘applicable property’ means any item which is—



1                   “(i) described in paragraph (1), (2),  
2                   (3), (5), (6), (7), or (8) of section 493(a)  
3                   (or any item substantially the same as any  
4                   such item), and

5                   “(ii) of a type which is actively trad-  
6                   ed.

7                   “(B) POSITION.—

8                   “(i) IN GENERAL.—The term ‘posi-  
9                   tion’ means an interest in applicable prop-  
10                  erty.

11                  “(ii) DERIVATIVES EXCLUDED.—Such  
12                  term shall not include a derivative (as de-  
13                  fined in section 493).

14                  “(C) STOCK AND DEBT WHOSE VALUE PRI-  
15                  MARILY DETERMINED BY REFERENCE TO  
16                  OTHER ITEMS.—Except as provided in regula-  
17                  tions, if the taxpayer holds an item described in  
18                  paragraph (1) or (3) of section 493(a) the value  
19                  of which, or with respect to which any payment  
20                  or other transfer, is primarily determined by  
21                  reference to one or more other items described  
22                  in paragraphs (1) through (8) of section  
23                  493(a), then, solely for purposes of this section,  
24                  such item described in paragraph (1) or (3) of

1 section 493(a) shall also be treated as if it were  
2 such other item.

3 “(5) POSITIONS HELD BY RELATED PERSONS,  
4 ETC.—

5 “(A) IN GENERAL.—In determining wheth-  
6 er 2 or more positions are offsetting, the tax-  
7 payer shall be treated as holding any position  
8 held by a related party (within the meaning of  
9 section 492(f)).

10 “(B) CERTAIN PASS-THROUGH ENTI-  
11 TIES.—If part or all of the gain or loss with re-  
12 spect to a position held by a partnership, trust,  
13 or other entity would properly be taken into ac-  
14 count for purposes of this chapter by a tax-  
15 payer, then, except to the extent otherwise pro-  
16 vided by the Secretary, such position shall be  
17 treated as held by the taxpayer.

18 “(6) SPECIAL RULES FOR FOREIGN CUR-  
19 RENCY.—

20 “(A) POSITION TO INCLUDE INTEREST IN  
21 CERTAIN DEBT.—For purposes of paragraph  
22 (4)(B)(i), an obligor’s interest in a nonfunc-  
23 tional currency denominated debt obligation is  
24 treated as a position in the nonfunctional cur-  
25 rency.

1                   “(B) ACTIVELY TRADED REQUIREMENT.—  
2                   For purposes of paragraph (4)(A)(ii), foreign  
3                   currency for which there is an active interbank  
4                   market is presumed to be actively traded.

5                   “(d) EXCEPTION FOR HEDGING TRANSACTIONS AND  
6 INVESTMENT HEDGING UNITS.—This section shall not  
7 apply in the case of—

8                   “(1) any hedging transaction (as defined in sec-  
9                   tion 1221(b)), and

10                   “(2) any investment hedging unit (as defined in  
11                   section 492).

12                   “(e) CROSS REFERENCE.—For provisions requiring  
13 capitalization of certain interest and carrying charges  
14 where there is a straddle, see section 263(g).”.

15                   (2) CONFORMING AMENDMENTS.—The last sen-  
16                   tence of section 246(c)(4) is amended—

17                   (A) by inserting “(as in effect before its re-  
18                   peal)” after “section 1092(c)(4)”, and

19                   (B) by inserting “(as so in effect)” after  
20                   “section 1092(f)”.

21                   (c) DEBT INSTRUMENTS HELD BY INSURANCE COM-  
22 PANIES.—

23                   (1) IN GENERAL.—Subsection (a) of section  
24                   1221 is amended by striking “or” at the end of  
25                   paragraph (7), by striking the period at the end of

1 paragraph (8) and inserting “; or”, and by adding  
2 at the end the following:

3 “(9) any bond, debenture, note, or certificate or  
4 other evidence of indebtedness held by an applicable  
5 insurance company (as defined in subsection  
6 (b)(5)).”.

7 (2) APPLICABLE INSURANCE COMPANY.—Sec-  
8 tion 1221(b), as amended by this Act, is amended  
9 by adding at the end the following:

10 “(5) APPLICABLE INSURANCE COMPANY.—For  
11 purposes of subsection (a)(9)—

12 “(A) IN GENERAL.—The term ‘applicable  
13 insurance company’ means, with respect to any  
14 taxable year, an insurance company (as defined  
15 in the last sentence of section 816(a))—

16 “(i) which is subject to tax under sec-  
17 tion 801(a) or section 831(a),

18 “(ii) with respect to which sections  
19 831(b), 835, and 842 do not apply, and

20 “(iii) which is not treated as a stock  
21 insurance company solely by reason of sec-  
22 tion 833(a)(1).

23 “(B) PERMANENT TREATMENT BY COM-  
24 PANY AS ORDINARY ASSET.—If an asset is  
25 treated as an asset described in subsection

1 (a)(9) with respect to any applicable insurance  
2 company for any taxable year, such asset shall  
3 be treated as so described during any subse-  
4 quent taxable year such asset is held by such  
5 company.”.

6 (3) REGULATIONS.—Paragraph (4) of section  
7 1221(b) is amended—

8 (A) by striking “The Secretary” and in-  
9 serting:

10 “(A) RELATED PARTIES.—The Secretary”,  
11 and

12 (B) by adding at the end the following:

13 “(B) ASSETS OF INSURANCE COMPA-  
14 NIES.—The Secretary shall prescribe such regu-  
15 lations as may be necessary or appropriate to  
16 carry out the purposes of subsection (a)(9), in-  
17 cluding such regulations as may be necessary to  
18 prevent the avoidance of Federal income tax  
19 through the sale or exchange of assets described  
20 in such subsection.”.

21 (4) EFFECTIVE DATE.—

22 (A) IN GENERAL.—The amendments made  
23 by this subsection shall apply to any bond, de-  
24 benture, note, or certificate or other evidence of  
25 indebtedness held or acquired after the 90-day

1 period beginning with the date of the enactment  
2 of this Act.

3 (B) TRANSITION RULE.—If a taxpayer has  
4 a capital loss carryover to any taxable year of  
5 the taxpayer beginning after the close of the  
6 90-day period described in subparagraph (A),  
7 the taxpayer shall, in addition to other short-  
8 term capital gain of the taxpayer (if any), treat  
9 as short-term capital gain (rather than as ordi-  
10 nary income) an amount equal to the lesser  
11 of—

12 (i) the net gain (if any) from sales or  
13 exchanges during such taxable year of as-  
14 sets to which section 1221(a)(9) of such  
15 Code (as added by paragraph (1)) applies,  
16 or

17 (ii) the capital loss carryovers to such  
18 taxable year from taxable years beginning  
19 before the close of such period.

20 (d) RICs ALLOWED NET OPERATING LOSS DEDUC-  
21 TION.—

22 (1) IN GENERAL.—Paragraph (2) of section  
23 852(b) is amended by striking subparagraph (B)  
24 and by redesignating subparagraphs (C) through (G)  
25 as subparagraphs (B) through (F), respectively.

1           (2) OTHER MODIFICATIONS.—Paragraph (6) of  
2 section 172(d) is amended to read follows:

3           “(6) MODIFICATIONS RELATED TO RICS AND  
4 REITS.—In the case of any taxable year for which  
5 part I or II of subchapter M applies to the tax-  
6 payer—

7           “(A) the net operating loss for such tax-  
8 able year shall be computed by taking into ac-  
9 count—

10           “(i) in the case of a regulated invest-  
11 ment company, the adjustments described  
12 in section 852(b)(2) (other than the deduc-  
13 tion for dividends paid described in sub-  
14 paragraph (C) thereof)), and

15           “(ii) in the case of a real estate in-  
16 vestment trust, the adjustments described  
17 in section 857(b)(2) (other than the deduc-  
18 tion for dividends paid described in sub-  
19 paragraph (B) thereof),

20           “(B) where such taxable year is a ‘prior  
21 taxable year’ referred to in paragraph (2) of  
22 subsection (b), references in such paragraph to  
23 ‘taxable income’ shall be treated as references  
24 to—

1           “(i) in the case of a regulated invest-  
2           ment company, regulated investment com-  
3           pany taxable income (as defined in section  
4           852(b)(2)), and

5           “(ii) in the case of a real estate in-  
6           vestment trust, real estate investment tax-  
7           able income (as defined in section  
8           857(b)(2)), and

9           “(C) subsection (a)(2) shall be applied by  
10          treating references to taxable income as ref-  
11          erences to—

12           “(i) in the case of a regulated invest-  
13           ment company, regulated investment com-  
14           pany taxable income (as defined in section  
15           852(b)(2)) but without regard to the de-  
16           duction for dividends paid (as defined in  
17           section 561), and

18           “(ii) in the case of a real estate in-  
19           vestment trust, real estate investment tax-  
20           able income (as defined in section  
21           857(b)(2)) but without regard to the de-  
22           duction for dividends paid (as defined in  
23           section 561).”.

24          (3) CONFORMING AMENDMENTS.—



1 (A) Section 443(e)(3) is amended by strik-  
2 ing “section 852(b)(2)(D)” and inserting “sec-  
3 tion 852(b)(2)(C)”.

4 (B) Section 852(a)(1)(A) is amended by  
5 striking “subsection (b)(2)(D)” and inserting  
6 “subsection (b)(2)(C)”.

7 (C) Section 4982(e)(1)(A) is amended by  
8 striking “and (D)” and inserting “and (C)”.

9 (4) EFFECTIVE DATE.—The amendments made  
10 by this subsection shall apply to net operating losses  
11 for taxable years ending after the 90th day after the  
12 date of the enactment of this Act.

13 (e) NONRECOGNITION OF GAIN OR LOSS FROM  
14 TRANSACTIONS BY A CORPORATION WITH RESPECT TO  
15 ITS STOCK.—

16 (1) IN GENERAL.—Section 1032 is amended to  
17 read as follows:

18 **“SEC. 1032. TRANSACTIONS BY A CORPORATION WITH RE-  
19 SPECT TO ITS STOCK.**

20 “(a) NONRECOGNITION ON EXCHANGE OF STOCK  
21 FOR PROPERTY.—No gain or loss shall be recognized to  
22 a corporation on the receipt of money or other property  
23 in exchange for stock of such corporation.

24 “(b) DERIVATIVE TRANSACTIONS BY A CORPORATION  
25 WITH RESPECT TO ITS STOCK.—

1           “(1) IN GENERAL.—Except as otherwise pro-  
2           vided in this subsection, section 1032 derivative  
3           items of a corporation shall not be taken into ac-  
4           count in determining such corporation’s liability for  
5           tax under this subtitle.

6           “(2) INCOME RECOGNITION ON CERTAIN FOR-  
7           WARD CONTRACTS.—

8           “(A) IN GENERAL.—If—

9                   “(i) a corporation acquires its stock,  
10                  and

11                   “(ii) such acquisition is part of a plan  
12                   (or series of related transactions) pursuant  
13                   to which the corporation enters into a for-  
14                   ward contract with respect to its stock,

15           such corporation shall include amounts in in-  
16           come as if the excess of the amount to be re-  
17           ceived under the forward contract over the fair  
18           market value of the stock as of the date the  
19           corporation entered into the forward contract  
20           were original issue discount on a debt instru-  
21           ment acquired on such date. The preceding sen-  
22           tence shall apply only to the extent that the  
23           amount of stock involved in the forward con-  
24           tract does not exceed the amount acquired as  
25           described in clause (i).

1           “(B) PLAN PRESUMED TO EXIST.—If a  
2           corporation enters into a forward contract with  
3           respect to its stock within the 60-day period be-  
4           ginning on the date which is 30 days before the  
5           date that the corporation acquires its stock,  
6           such acquisition shall be treated as pursuant to  
7           a plan described in subparagraph (A)(ii) unless  
8           it is established that entering into such contract  
9           and such acquisition are not pursuant to a plan  
10          or series of related transactions.

11          “(c) SECTION 1032 DERIVATIVE ITEMS.—For pur-  
12         poses of this section, the term ‘section 1032 derivative  
13         item’ means, with respect to any corporation, any item of  
14         income, gain, loss, or deduction if—

15                 “(1) such item arises out of the rights or obli-  
16                 gations under any derivative (as defined in section  
17                 493) to the extent such derivative relates to the cor-  
18                 poration’s stock (or is attributable to any transfer or  
19                 extinguishment of any such right or obligation), or

20                 “(2) such item arises under any other contract  
21                 or position but only to the extent that such item re-  
22                 flects (or is determined by reference to) changes in  
23                 the value of such stock or distributions thereon.

24         Such term shall not include any deduction with respect  
25         to which section 83(h) applies and shall not include any

1 deduction for any item which is in the nature of compensa-  
2 tion for services rendered. For purposes of this subpara-  
3 graph, de minimis relationships, as determined by the Sec-  
4 retary, shall be disregarded.

5 “(d) COORDINATION WITH DERIVATIVE AND STRAD-  
6 DLE RULES.—In the case of a derivative or other contract  
7 or position described in subsection (c) which is held by  
8 a corporation with respect to its stock—

9 “(1) this section (rather than part IV of sub-  
10 chapter E or section 1092) shall apply in deter-  
11 mining the treatment of section 1032 derivative  
12 items under this subtitle, and

13 “(2) such derivative or other contract or posi-  
14 tion shall not be taken into account in determining  
15 whether the corporation has an investment hedging  
16 unit, applicable property interest, or straddle with  
17 respect to its stock for purposes of such part or sec-  
18 tion.

19 “(e) REGULATIONS.—The Secretary shall prescribe  
20 such regulations or other guidance as may be appropriate  
21 to carry out the purposes of this section, including regula-  
22 tions or other guidance which treat the portion of an in-  
23 strument which is described in subsection (c)(1) separately  
24 from the portion of such instrument which is not so de-  
25 scribed.

1       “(f) BASIS.—For basis of property acquired by a cor-  
2 poration in certain exchanges for its stock, see section  
3 362.”.

4           (2) CLERICAL AMENDMENT.—The item relating  
5 to section 1032 in the table of sections for part III  
6 of subchapter O of chapter 1 is amended to read as  
7 follows:

“Sec. 1032. Transactions by a corporation with respect to its stock.”.

8           (3) EFFECTIVE DATE.—The amendments made  
9 by this subsection shall apply to transactions entered  
10 into after the date of the enactment of this Act.

11 **SEC. 4. TECHNICAL AND CONFORMING AMENDMENTS.**

12       (a) REPEAL OF CERTAIN OTHER SUPERCEDED  
13 RULES FOR DETERMINING CAPITAL GAINS AND  
14 LOSSES.—

15           (1) IN GENERAL.—Part IV of subchapter P of  
16 chapter 1 is amended by striking sections 1233,  
17 1234, 1234A, 1234B, 1236, 1256, 1258, 1259, and  
18 1260 (and by striking the items relating to such sec-  
19 tions in the table of sections for such part).

20           (2) CONFORMING AMENDMENTS RELATED TO  
21 REPEAL OF SECTION 1234.—Section 6045(h)(2) is  
22 amended—

23           (A) by striking “(as defined in section  
24 1234(b)(2)(A))”, and

1 (B) by adding at the end the following:

2 “For purposes of the preceding sentence, the  
3 term ‘closing transaction’ means any termi-  
4 nation of the taxpayer’s obligation under an op-  
5 tion in property other than through the exercise  
6 or lapse of the option.”.

7 (3) CONFORMING AMENDMENTS RELATED TO  
8 REPEAL OF SECTION 1236.—

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

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

14 (C) Section 1058 is amended—

15 (i) by striking “(as defined in section  
16 1236(c))” in subsection (a), and

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

20 “(c) SECURITIES.—For purposes of this section, the  
21 term ‘security’ means any share of stock in any corpora-  
22 tion, certificate of stock or interest in any corporation,  
23 note, bond, debenture, or evidence of indebtedness, or any  
24 evidence of an interest in or right to subscribe to or pur-  
25 chase any of the foregoing.”.

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

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

5           “(B) any partnership or other entity (other  
6 than a corporation which is not an S corpora-  
7 tion) if more than 35 percent of the losses of  
8 such entity during the taxable year are allocable  
9 to limited partners or limited entrepreneurs  
10 (within the meaning of subsection (k)(4)),  
11 and”.

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

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

17           (D) Section 1212 is amended by striking  
18 subsection (c).

19           (E) Section 1223 is amended by striking  
20 paragraphs (7) and (14).

21           (F) Section 1281(b)(1)(E) is amended to  
22 read as follows:

23           “(E) is part of a hedging transaction (as  
24 defined in section 1221(b)) or an investment  
25 hedging unit (as defined in section 492), or”.

1 (G) Section 1402 is amended by striking  
2 subsection (i).

3 (H) Section 4982(e)(6)(B) is amended by  
4 striking “sections 1256 and 1296” and insert-  
5 ing “sections 491 and 1296”.

6 (5) CONFORMING AMENDMENTS RELATED TO  
7 REPEAL OF SECTION 1259.—Section 475(f)(1) is  
8 amended by striking subparagraph (C) and by redese-  
9 ignating subparagraph (D) as subparagraph (C).

10 (b) OTHER CONFORMING AMENDMENTS.—

11 (1) Section 355(g)(2)(B)(i)(V) is amended to  
12 read as follows:

13 “(V) any derivative (as defined in  
14 section 493),”.

15 (2) Section 856(n)(4) is amended by inserting  
16 “or derivatives (as defined in section 493)” after  
17 “securities (as defined in section 475(e)(2))”.

18 (3) Section 857(e)(2)(C)(i) is amended by strik-  
19 ing “section 860E or 1272” and inserting “section  
20 491, 860E, or 1272”.

21 (4) Section 988(d)(1) is amended—

22 (A) by striking “or 1256” and inserting  
23 “or 491”, and

24 (B) by striking “1092, and 1256” and in-  
25 serting “491, and 1092”.



1           (5) Section 1091(e) is amended to read as fol-  
2           lows:

3           “(e) COORDINATION WITH MARK TO MARKET OF  
4           DERIVATIVES AND UNDERLYING INVESTMENTS.—For  
5           purposes of this section, the term ‘stock or securities’ shall  
6           not include—

7           “(1) any derivative (as defined in section 493),  
8           or

9           “(2) any underlying investment (as defined in  
10          section 492(e)(1)) which, at the time of the sale or  
11          other disposition, is part of an investment hedging  
12          unit (as defined in section 492).”.

13          (6)(A) Section 1221(a)(6) is amended to read  
14          as follows:

15          “(6) any—

16                 “(A) derivative (as defined in section 493),

17                 or

18                 “(B) any underlying investment (as de-  
19                 fined in section 492(e)(1)) which is part of an  
20                 investment hedging unit (as defined in section  
21                 492),”.

22          (B) Section 1221(b) is amended by striking  
23          paragraph (1).

1           (7) Section 4975(f)(11)(D) is amended by  
2 striking clauses (i) and (ii) and inserting the fol-  
3 lowing:

4                   “(i) SECURITY.—The term ‘security’  
5 means any security described in section  
6 475(e)(2) (without regard to subparagraph  
7 (D)(iii) thereof) and any derivative with re-  
8 spect to such a security (within the mean-  
9 ing of section 493).

10                   “(ii) COMMODITY.—The term ‘com-  
11 modity’ means any commodity described in  
12 section 475(e)(2) (without regard to sub-  
13 paragraph (B)(iii) thereof) and any deriva-  
14 tive with respect to such a commodity  
15 (within the meaning of section 493).”.

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

“PART IV. TAX TREATMENT OF DERIVATIVES AND SIMILAR CONTRACTS”.

19 **SEC. 5. EFFECTIVE DATES.**

20           (a) IN GENERAL.—Except as provided in this Act—

21                   (1) the amendments made by section 2 shall  
22 apply to taxable events occurring after the 90-day  
23 period beginning with the date of the enactment of  
24 this Act, in taxable years ending after the last day  
25 of such period, and

1           (2) the amendments made by sections 3 and 4  
2           shall apply to derivatives and underlying investments  
3           held after the last day of such period.

4           (b) IDENTIFICATION REQUIREMENTS.—If, as of the  
5           close of the 90-day period described in subsection (a)(1),  
6           a taxpayer simultaneously holds 1 or more derivatives with  
7           respect to an underlying investment and the underlying  
8           investment—

9           (1) the taxpayer shall make the identifications  
10          required under section 492(c)(2) of Internal Rev-  
11          enue Code of 1986 (as added by section 2 of this  
12          Act) before the close of such period, and

13          (2) if such identifications result in an invest-  
14          ment hedging unit, the first applicable hedging pe-  
15          riod with respect to such unit shall begin on the day  
16          after the close of such period.

17          (c) DEFINITIONS.—For purposes of this section, any  
18          term used in this section which is also used in part IV  
19          of subchapter E of chapter 1 of such Code (as so added)  
20          shall have the same meaning as when used in such part.