SECTION 402. TREATMENT OF QUALIFYING DIRECTOR SHARES

The Act clarifies that qualifying director shares of bank are not to be treated as a second class of stock. Instead, the qualifying director shares are treated as a liability of the bank and no income or loss from the S corporation will be allocated to these qualifying director shares. The provision clarifies the law and removes a significant obstacle unique among banks contemplating a S corporation election.

SECTION 403. BAD DEBT CHARGE OFFS IN YEARS AFTER ELECTION YEAR TREATED AS ITEMS OF BUILT-IN LOSS

The Act permits bank S corporations to recapture up to 100 percent of their bad debt reserves on their first S corporation tax return and/or their last C corporation income tax return prior to the effective date of the S election. Banks that convert to S corporation status must change from the reserve method of accounting to the specific charge off method. The resulting recapture income is treated as built-in gain subject to tax at both the shareholder and the corporate level. The Act allows banks to accelerate the recapture of bad debt reserve to their last C corporation tax year. The corporate level tax would still be paid on the recapture income, but the recapture would no longer trigger a tax for the bank's shareholders.

TITLE V—QUALIFIED SUBCHAPTER S SUBSIDIARIES

SECTION 501. RELIEF FROM INADVERTENTLY INVALID QUALIFIED SUBCHAPTER S SUBSIDIARY ELECTIONS AND TERMINATIONS.

The Act provides statutory authority for the Secretary to grant relief for invalid QSub elections, and terminations of QSub status, if the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent. This would allow the IRS to provide relief in appropriate cases, just as it currently does in the case of invalid or ten-ninated S corporation elections.

SECTION 502. INFORMATION RETURNS FOR QUALIFIED SUBCHAPTER S SUBSIDIARIES

The Act would help clarify that a Qualified Subchapter S Subsidiary (QSSS) can provide information returns under their own tax ID number to help avoid confusion by employers, depositors, and other parties.

SECTION 503. TREATMENT OF THE SALE OF INTEREST IN A QUALIFIED SUBCHAPTER S SUBSIDIARY

The Act treats the disposition of QSub stock as a sale of the undivided interest in the QSub's assets based on the underlying percentage of stock transferred followed by a deemed contribution by the S corporation and the acquiring party in a nontaxable transaction. Under current law, an S corporation may be required to recognize 100 percent of the gain inherent in a QSub's assets if it sells as little as 21 percent of the QSub's stock. IRS regulations suggest this result can be avoided by merging the QSub into a single member LLC prior to the sale, then selling an interest in the LLC (as opposed to stock in the QSub). The Act achieves this result without any unnecessary merger and thus removes a trap for the unwary.

SECTION 504. EXCEPTION TO APPLICATION OF STEP TRANSACTION DOCTRINE FOR RESTRUCTURING IN CONNECTION WITH MAKING QUALIFIED SUBCHAPTER S SUBSIDIARY ELECTIONS

The Act provides that the step transaction doctrine does not apply to the deemed liquidation resulting from QSub elections. Application of the step transaction doctrine, in the context of making a QSub election, introduces complexity and uncertainty in what should be a simple matter. The doctrine requires knowledge of decades of jurisprudence and administrative interpretations, and poses an unnecessary trap for the unwary.

TITLE VI—ADDITIONAL PROVISIONS

SECTION 601. ELIMINATION OF ALL EARNINGS AND PROFITS ATTRIBUTABLE TO PRE-1983 YEARS

The Small Business Job Protection Act of 1996 eliminated certain pre-1983 earnings and profits of S corporations that had S corporation status for their first tax year beginning after December 31, 1996. This provision should apply to all corporations (C and S) with pre-1983 S earnings and profits without regard to when they elect S status. There seems to be no policy reason why the elimination was restricted to corporations with an S election in effect for their first taxable year beginning after December 31, 1996.

SECTION 602. NO GAIN OR LOSS ON DEFERRED INTERCOMPANY TRANSACTIONS BECAUSE OF CONVERSION TO S CORPORATION OR QUALIFIED S CORPORATION SUBSIDIARY

The Act makes clear that any gain or income from an intercompany transaction is not taxed at the time of the S corporation or QSub elections.

SECTION 603. TREATMENT OF CHARITABLE CONTRIBUTION AND FOREIGN TAX CREDIT CARRYFORWARDS

The Act provides that charitable contribution carryforwards and other carryforwards arising from a taxable year for which the corporation was a C corporation shall be allowed as a deduction against the net recognized built-in gain of the corporation for the taxable year. This provision is consistent with the legislative history of the 1986 Act.

SECTION 604. DISTRIBUTION BY AN S CORPORATION TO AN EMPLOYEE STOCK OWNERSHIP PLAN

An ESOP will usually borrow from the sponsoring corporation to fund its acquisition of employer securities. In the case of a C corporation, the tax code provides that an ESOP will not be treated as engaging in a ''prohibited transaction'' if it uses any ''dividend'' on employer securities purchased with loan proceeds to make payments on the loan regardless of whether such employer securities have been pledged as collateral to secure the loan. The policy facilitates the payment of ESOP loans and thereby promotes employee ownership. Because S corporation distributions are technically not ''dividends'', the Act provides that S corporation distributions are treated as dividends. This clarification is necessary to ensure that the policy of facilitating the payment of ESOP loans applies equally to S corporation and C corporation ESOPs.

SECTION 605. SPECIAL RULES OF APPLICATION

The effective dates of some amendments made by the Act may occur in years in which it is too late to file a claim for refund arising in such years from applying the amendments. The Act grants a 1-year extension beginning on the date of enactment in which to file such claims for these closed years.

Mr. Speaker, I urge my fellow members to review and support the S Corporation Modernization Act, which will help create a level playing field for small businesses. I look forward to working with my colleagues on the Ways and Means Committee to enact this bill.

GIVING PRAISE TO ZION EVANGELICAL LUTHERAN CHURCH

HON. JAMES A. BARCIA

OF MICHIGAN

IN THE HOUSE OF REPRESENTATIVES

Thursday, July 19, 2001

Mr. BARCIA. Mr. Speaker, I rise today to sing the praises of Zion Evangelical Lutheran Church in Bay City, Michigan, as Reverend William H. Allwardt, his family and the congregation celebrate the 100th anniversary of its founding. Since its humble beginnings in 1901 in a small wood-frame building, Zion has grown to become a stronghold of faith for over 2,000 members in and around Bay City.

In 1901, Zion members first gathered to worship in a wooden building that once had been the Salzburg Band Hall. As the congregation grew, so did the need for a larger forum, resulting in the building in November 1930 of the present-day church. From the beginning, church leaders also recognized that religious education doesn't take place only on Sundays, so they built a schoolhouse. The commitment to Christian education continues today inside the Zion Memorial Building, named to honor the men and women of Zion who served in World War II. During the last school year, 170 students studied and learned at Zion.

Tradition and a sense of continuity have always been important elements in Zion's spiritual mission. In keeping with those practices, the church has had just seven pastors in a century's time. The present pastor, Reverend Allwardt, his wife, Paulette, and children, Will and Charice, have been part of the Zion family since 1978 and have contributed greatly to its rich history and Christian undertaking to spread the word of God to people near and far.

A fruitful church cannot multiply the ranks of the faithful without reaching out and Zion's congregation has always opened its doors and expanded its influence well beyond the sanctuary and into the surrounding community. Over the years, Zion has led by Christian example with their involvement in many social organizations, including the Saginaw Valley Blood Program, the Boy Scouts and Girl Scouts of America, the Bay County Food Pantry and the CROP Walk.

Mr. Speaker, I ask my colleagues to join me in honoring Zion Evangelical Lutheran Church for a century of Christian service, fellowship and leadership from the pulpit, the pews and among the greater community and in wishing them another hundred years of success.

SALUTE TO VERNA SMALL

HON. JERROLD NADLER

OF NEW YORK

IN THE HOUSE OF REPRESENTATIVES

Thursday, July 19, 2001

Mr. NADLER. Mr. Speaker, I rise today to laud the incredible and enduring community activism of Verna Small. Verna has been active in the Greenwich Village community of New York City for over half a century, however she got her start right here in Washington, D.C. A 1937 graduate of George Washington University, Verna soon began working for the United States Department of