

**DESCRIPTION OF REVENUE PROVISIONS  
TO BE CONSIDERED  
IN CONNECTION WITH A MARKUP OF  
TRADE MATTERS**

Scheduled for Markup

by the

SENATE COMMITTEE ON FINANCE

on

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Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

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## INTRODUCTION

This document<sup>1</sup>, prepared by the staff of the Joint Committee on Taxation, contains a description of revenue proposals to be considered by the Senate Committee on Finance in connection with a markup of trade matters, scheduled for July 21, 1998.

This document contains descriptions of the following revenue proposals: (1) the modification of the foreign tax credit carryback and carryover periods, and (2) the expansion of the definition of vessels qualified for capital construction fund treatment.

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<sup>1</sup> This document may be cited as follows: Joint Committee on Taxation *Description of Revenue Provisions to be Considered in Connection with a Markup of Trade Matters* (JCX-54-98), July 20, 1998.

## DESCRIPTION OF REVENUE PROVISIONS

### 1. Modification to Foreign Tax Credit Carryback and Carryover Periods

#### Present Law

U.S. persons may credit foreign taxes against U.S. tax on foreign-source income. The amount of foreign tax credits that can be claimed in a year is subject to a limitation that prevents taxpayers from using foreign tax credits to offset U.S. tax on U.S.-source income. Separate foreign tax credit limitations are applied to specific categories of income.

The amount of creditable taxes paid or accrued (or deemed paid) in any taxable year which exceeds the foreign tax credit limitation is permitted to be carried back two years and forward five years. The amount carried over may be used as a credit in a carryover year to the extent the taxpayer otherwise has excess foreign tax credit limitation for such year. The separate foreign tax credit limitations apply for purposes of the carryover rules.

#### Description of Proposal

The proposal would reduce the carryback period for excess foreign tax credits from two years to one year. The proposal also would extend the excess foreign tax credit carryforward period from five years to seven years.

#### Effective Date

The proposal would apply to foreign tax credits arising in taxable years beginning after December 31, 1998.

### 2. Expansion of Definition of Vessels Qualified for Capital Construction Fund Treatment

#### Present Law

Under section 7518 of the Internal Revenue Code (the "Code"), in determining taxable income for regular tax purposes, a qualified taxpayer who owns or leases a qualified vessel (an "agreement vessel") is allowed a deduction for certain amounts contributed to a fund established under section 607 of the Merchant Marine Act, 1936 (a "capital construction fund"). In addition, the investment earnings on amounts contributed to a capital construction fund are excluded from gross income for regular tax purposes.

If a withdrawal from a capital construction fund is used to acquire, construct, or reconstruct a qualified vessel, the amount withdrawn generally is not included in gross income and the basis of the qualified vessel generally is reduced by the amount withdrawn to the extent attributable to

amounts previously deducted or excluded from income. In the case of any other withdrawal from a capital construction fund, the amount withdrawn generally is included in gross income to the extent attributable to amounts previously deducted or excluded from income and interest on the tax liability attributable to such inclusion generally must be paid from the date of the deduction or exclusion.

Any term (including the definition of "agreement vessel") provided in section 607(k) of the Merchant Marine Act, 1936, as in effect as of the date of enactment of the Tax Reform Act of 1986, applies for purposes of section 7518. Under section 607(k) of the Merchant Marine Act, 1936, as in effect as of the date of enactment of the Tax Reform Act of 1986, an agreement vessel generally is a vessel constructed or reconstructed in the United States (the "U.S.-build requirement") and documented under the laws of the United States (the "U.S.-flag requirement"). In addition, the person maintaining the capital construction fund must agree with the Secretary (of Commerce or Transportation) that the vessel will be operated in the United States foreign trade, Great Lakes trade, or noncontiguous domestic trade or in the fisheries of the United States.

### **Description of Proposal**

The proposal would provide that any term provided in section 607(k) of the Merchant Marine Act, 1936, as in effect as of the date that the OECD Shipbuilding Trade Agreement Act enters into force with respect to the United States, would apply for purposes of section 7518 of the Code. Thus, in general, for purposes of the tax benefits provided by capital construction funds, an agreement vessel would include any vessel constructed or reconstructed in any nation that is a signatory to the OECD shipbuilding agreement entered into on December 21, 1994. In effect, the proposal would eliminate the "U.S.-build requirement" of present law for vessels constructed or reconstructed in a signatory nation.

### **Effective Date**

The proposal would be effective as of the date that the OECD Shipbuilding Trade Agreement Act enters into force with respect to the United States.