COMPARISON OF CERTAIN PROVISIONS OF H.R. 4520 AS PASSED BY THE HOUSE OF REPRESENTATIVES AND AS AMENDED BY THE SENATE:

PROVISIONS RELATING TO INTERNATIONAL TAX REFORM AND SIMPLIFICATION FOR UNITED STATES BUSINESSES

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JOINT COMMITTEE ON TAXATION

September 29, 2004
JCX-63-04

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INTRODUCTION

On June 17, 2004, the House of Representatives passed H.R. 4520, the "American Jobs Creations Act of 2004." On July 15, 2004, the Senate amended H.R. 4520 by substituting the text and title of S. 1637, the "Jumpstart Our Business Strength (JOBS) Act,"[1] and an additional non-tax amendment.

The House bill and the Senate amendment each repeal the extraterritorial income exclusion provisions of present law, provide provisions to reduce the effective income tax imposed on income earned from certain domestic production activities, and make numerous other changes to the Internal Revenue Code. This document,[2] prepared by the staff of the Joint Committee on Taxation, compares certain provisions relating to international tax reform and simplification for United States businesses.

In this publication set,[3] (JCX-61-04 to JCX-66-04), the staff of the Joint Committee on Taxation compares provisions of H.R. 4520 as passed by the House of Representatives and as amended by the Senate relating to the repeal of the extraterritorial income

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[1] The Senate originally passed S. 1637 on May 11, 2004.

[2] This document may be cited as follows: Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Provisions Relating to International Tax Reform and Simplification for United States Businesses* (JCX-63-04), September 29, 2004.

[3] Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Provisions Relating to the Repeal of the Exclusion for Extraterritorial Income, Domestic Production, and the Corporate Income Tax Rates Applicable to Small Corporations* (JCX-61-04), September 29, 2004; Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Job Creation Tax Incentives for Manufacturing, Small Business, and Farming* (JCX-62-04), September 29, 2004; Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Provisions Relating to International Tax Reform and Simplification for United States Businesses* (JCX-63-04), September 29, 2004; Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Revenue Provisions* (JCX-64-04), September 29, 2004; Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Alcohol Fuels and Fuel Fraud Provisions* (JCX-65-04), September 29, 2004; and Joint Committee on Taxation, *Comparison of Certain Provisions of H.R. 4520 as Passed by the House of Representatives and as Amended by the Senate: Expiring Provisions* (JCX-66-04), September 29, 2004.

exclusions, domestic production, corporate income tax rates applicable to small corporations, tax incentives for manufacturers, small businesses and farming, international tax reform and simplification for United States businesses, alcohol fuels and fuel fraud, expiring provisions, and certain revenue raising provisions.

Provision	Present Law	House Bill	Senate Amendment
1. Interest expense allocation rules (sec. 301 of the House bill and sec. 205 of the Senate amendment)	In order to compute the foreign tax credit limitation, a taxpayer must determine the amount of its taxable income from foreign sources. In so doing, the taxpayer must allocate and apportion deductions between U.S.-source gross income and foreign-source gross income. In the case of interest expense, the rules generally are based on the approach that money is fungible and that interest expense is properly attributable to all assets of a taxpayer, regardless of any specific purpose for incurring the underlying obligation. This fungibility principle is applied on a "water's edge" basis, under which the U.S. interest expense of a multinational group is effectively deemed to support both U.S. and foreign assets of the group, but the interest expense of foreign group members is disregarded for this purpose. As a result, some of the group's U.S. interest expense will reduce foreign-source income, even in cases in which foreign group members borrow locally at levels appropriate to support their assets.	Provides a one-time election under which the taxable income of the domestic members of an affiliated group from sources outside the United States generally is determined by allocating and apportioning interest expense of the domestic members of a worldwide affiliated group on a worldwide-group basis (a "worldwide fungibility" approach). If a group makes this election, the third-party interest expense of domestic group members is allocated and apportioned to foreign-source income in an amount equal to the excess (if any) of: (1) the group's worldwide third-party interest expense multiplied by the ratio which the foreign assets of the worldwide affiliated group bears to the total assets of the worldwide affiliated group; over (2) the third-party interest expense incurred by foreign group members to the extent such interest would be allocated to foreign sources if the provision's principles were applied separately to the foreign members of the group.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	A "financial corporation" is not treated as a member of the regular affiliated group for purposes of applying the allocation and apportionment rules to non-financial members of that group. Instead, all financial corporations that would be so affiliated are treated as a separate single corporation for these purposes.	The bill also allows taxpayers to apply the present-law financial group rules to exclude certain financial institutions from the affiliated group for interest allocation purposes. In addition, the bill provides a one-time "financial institution group" election that expands the present-law bank group. <u>Effective date</u>.–Taxable years beginning after December 31, 2008.	
2. Recharacterize overall domestic loss (sec. 302 of the House bill and sec. 204 of the Senate amendment)	If a taxpayer's losses from foreign sources exceed its foreign-source income, the excess ("overall foreign loss," or "OFL") may offset U.S.-source income. Such an offset reduces the effective rate of U.S. tax on U.S.-source income. Under present law, a portion of foreign-source taxable income earned after an OFL year is recharacterized as U.S.-source taxable income for foreign tax credit purposes. The effect of this recapture is to reduce the foreign tax credit limitation in one or more years following an OFL year and, therefore, the amount of U.S. tax	The House bill applies a re-sourcing rule to U.S.-source income in cases in which a taxpayer's foreign tax credit limitation has been reduced as a result of an overall domestic loss. Under the provision, a portion of the taxpayer's U.S.-source income for each succeeding taxable year is recharacterized as foreign-source income in an amount equal to the lesser of: (1) the amount of the unrecharacterized overall domestic losses for years prior to such succeeding taxable year, and (2) 50 percent of the taxpayer's U.S.-source income for such succeeding taxable year.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	that can be offset by foreign tax credits in the later year or years. A U.S.-source loss reduces pre-credit U.S. tax on worldwide income to an amount less than the hypothetical tax that would apply to the taxpayer's foreign-source income viewed in isolation, thus reducing the foreign tax credit limitation. The existence of foreign-source taxable income in the year of the U.S.-source loss also reduces or eliminates any net operating loss carryover that the U.S.-source loss would otherwise have generated. There is currently no mechanism for recharacterizing subsequent U.S.-source income as foreign-source income, to correspond with the treatment of OFLs.	Any U.S.-source income recharacterized under the provision is allocated among and increases the various foreign tax credit separate limitation categories in the same proportion that those categories were reduced by the prior overall domestic losses, in a manner similar to the recharacterization rules for separate limitation losses. Effective date.–Losses incurred in taxable years beginning after December 31, 2006.	
3. Foreign tax credit baskets and base differences (sec. 303 of the House bill and sec. 225 of the Senate amendment)	Number of foreign tax credit baskets.–The foreign tax credit limitation is applied separately to the following categories of income: (1) passive income; (2) high withholding tax interest; (3) financial services income; (4) shipping income; (5) certain dividends received from	Number of foreign tax credit baskets.–The House bill generally reduces the number of foreign tax credit limitation categories to two: passive category income and general category income. Other income is included in one of the two categories, as appropriate. For example, shipping income	Number of foreign tax credit baskets.–No provision.

Provision	Present Law	House Bill	Senate Amendment
	noncontrolled section 902 foreign corporations ("10/50 companies"); (6) certain dividends from a domestic international sales corporation or former domestic international sales corporation; (7) taxable income attributable to certain foreign trade income; (8) certain distributions from a foreign sales corporation or former foreign sales corporation; and (9) any other income not described in items (1) through (8) (so-called "general basket" income).	generally falls into the general limitation category, whereas high withholding tax interest generally could fall into the passive income or the general limitation category, depending on the circumstances. Dividends from a domestic international sales corporation or former domestic international sales corporation, income attributable to certain foreign trade income, and certain distributions from a foreign sales corporation or former foreign sales corporation all are assigned to the passive income limitation category. In the case of a member of a financial services group or any other person predominantly engaged in the active conduct of a banking, insurance, financing or similar business, the bill treats income meeting the definition of financial services income as general category income.	
	<u>Base differences</u>.–Under Treasury regulations, foreign taxes are allocated and apportioned to the same limitation categories as the income to which they relate. In cases in which foreign law imposes tax on an item of income that does	<u>Base differences</u>.–Creditable foreign taxes that are imposed on amounts that do not constitute income under U.S. tax principles are treated as imposed on general limitation income.	<u>Base differences</u>.–The Senate amendment provides that creditable foreign taxes imposed on amounts that do not constitute income under U.S. tax principles are treated as imposed on general limitation income or on financial services

Provision	Present Law	House Bill	Senate Amendment
	not constitute income under U.S. tax principles (a "base difference" item), the tax is treated as imposed on income in the general limitation category.	Effective date.–Taxable years beginning after December 31, 2006.	income, at the taxpayer's election. Once made, this election also applies for all subsequent taxable years unless revoked with the consent of the Treasury Secretary. Effective date.–Taxable years ending after date of enactment.
4. Apply look-through rules for dividends from noncontrolled section 902 corporations (sec. 304 of the House bill and sec. 202 of the Senate amendment)	Special foreign tax credit limitations apply in the case of dividends received from a foreign corporation in which the taxpayer owns at least 10 percent of the stock by vote and which is not a controlled foreign corporation (a so-called "10/50 company"). Dividends paid by a 10/50 company that is not a passive foreign investment company out of earnings and profits accumulated in taxable years beginning before January 1, 2003, are subject to a single foreign tax credit limitation for all 10/50 companies (other than passive foreign investment companies). Dividends paid by a 10/50 company that is a passive foreign investment company out of earnings and profits accumulated in	Generally applies the look-through approach to dividends paid by a 10/50 company regardless of the year in which the earnings and profits out of which the dividend is paid were accumulated. Effective date.–Taxable years beginning after December 31, 2002.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	taxable years beginning before January 1, 2003, continue to be subject to a separate foreign tax credit limitation for each such 10/50 company. Dividends paid by a 10/50 company out of earnings and profits accumulated in taxable years after December 31, 2002 are treated as income in a foreign tax credit limitation category in proportion to the ratio of the 10/50 company's earnings and profits attributable to income in such foreign tax credit limitation category to its total earnings and profits (a "look-through" approach).		
5. Attribution of stock ownership through partnerships in determining section 902 and 960 credits (sec. 305 of the House bill and sec. 213 of the Senate amendment)	Under section 902, a domestic corporation that receives a dividend from a foreign corporation in which it owns ten percent or more of the voting stock is deemed to have paid a portion of the foreign taxes paid by such foreign corporation. Thus, such a domestic corporation is eligible to claim a foreign tax credit with respect to such deemed-paid taxes. The domestic corporation that receives a dividend is deemed to have paid a portion of the foreign corporation's post-1986 foreign	Clarifies that a domestic corporation is entitled to claim deemed-paid foreign tax credits with respect to a foreign corporation that is held indirectly through a foreign or domestic partnership, provided that the domestic corporation owns (indirectly through the partnership) ten percent or more of the foreign corporation's voting stock. The proposal also clarifies that both individual and corporate partners (or estate or trust beneficiaries) may claim direct foreign tax credits	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	income taxes based on the ratio of the amount of the dividend to the foreign corporation's post-1986 undistributed earnings and profits. The Code does not specifically address whether a domestic corporation owning ten percent or more of the voting stock of a foreign corporation through a partnership is entitled to a deemed-paid foreign tax credit.	with respect to their proportionate shares of taxes paid or accrued by a partnership (or estate or trust). <u>Effective date.</u>–Taxes of foreign corporations for taxable years of such corporations beginning after the date of enactment.	
6. Foreign tax credit treatment of deemed payments under section 367(d) (sec. 306 of the House bill and sec. 229 of the Senate amendment)	Under section 367(d) of the Code, the outbound transfer of intangible property by means of contribution and certain other nonrecognition transactions is treated as a sale of the intangible for a stream of contingent payments. The amounts of these deemed payments must be commensurate with the income attributable to the intangible. The amounts are sourced like royalties, but the Code does not clearly address how to characterize the amounts for purposes of applying the separate limitation categories of the foreign tax credit.	Specifies that deemed payments under section 367(d) are treated as royalties for purposes of applying the separate limitation categories of the foreign tax credit. <u>Effective date.</u>–Amounts treated as received on or after August 5, 1997.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
7. United States property not to include certain assets of controlled foreign corporations (sec. 307 of the House bill and sec. 227 of the Senate amendment)	U.S. 10-percent shareholders of a CFC generally are subject to U.S. tax currently on their pro rata shares of the controlled foreign corporations ("CFC's") earnings that have not previously been taxed in the United States, to the extent such earnings are invested by the CFC in certain U.S. property, including tangible property located in the United States, stock of a U.S. corporation, an obligation of a U.S. person, and certain intangible assets (e.g., patents or copyrights, inventions, models or designs, secret formulae or processes or similar property rights acquired or developed by the CFC for use in the United States). Specified exceptions from the definition of U.S. property are provided for, including: (1) stock or debt of certain unrelated U.S. corporations; and (2) certain deposits or receipts of collateral or margin by a securities or commodities dealer.	Adds two new exceptions from the definition of U.S. property for determining current income inclusion by a U.S. 10-percent shareholder with respect to an investment in U.S. property by a controlled foreign corporation. The first exception generally applies to securities acquired and held by a controlled foreign corporation in the ordinary course of its trade or business as a dealer in securities. The second exception generally applies to the acquisition by a controlled foreign corporation of obligations issued by an unrelated U.S. person that is not a domestic corporation. Effective date.–Taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders with or within which such taxable years of foreign corporations end.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
8. Election not to use average exchange rate for foreign tax paid other than in functional currency (sec. 308 of the House bill and sec. 224 of the Senate amendment)	For taxpayers that take foreign income taxes into account when accrued, the amount of the foreign tax credit generally is determined by translating the amount of foreign taxes paid in foreign currencies into a U.S. dollar amount at the average exchange rate for the taxable year to which such taxes relate. Foreign taxes that are not eligible for translation at the average exchange rate generally are translated into U.S. dollar amounts using the exchange rates as of the time such taxes are paid. However, the Secretary is authorized to issue regulations that would allow foreign tax payments to be translated into U.S. dollar amounts using an average exchange rate for a specified period.	For taxpayers that are required under present law to translate foreign income tax payments at the average exchange rate, provides an election to translate such taxes into U.S. dollar amounts using the exchange rates as of the time such taxes are paid, provided the foreign income taxes are denominated in a currency other than the taxpayer's functional currency. Any such election applies to the taxable year for which the election is made and to all subsequent taxable years unless revoked with the consent of the Secretary. <u>Effective date</u>.–Taxable years beginning after December 31, 2004.	Same as the House bill.
9. Eliminate secondary withholding tax with respect to dividends paid by certain foreign corporations (sec. 309 of the House bill and sec. 215 of the Senate amendment)	Foreign persons are subject to a 30-percent gross basis tax, collected by withholding, on certain U.S.-source passive income (e.g., dividends) that is not effectively connected with a U.S. trade or business. This withholding tax	Repeals the secondary withholding tax. <u>Effective date</u>.–Payments made after December 31, 2004.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	may be reduced or eliminated by treaty. In general, dividends paid by a domestic corporation are treated as U.S.-source, and dividends paid by a foreign corporation are treated as foreign-source. However, if a foreign corporation derives 25 percent or more of its gross income as income effectively connected with a U.S. trade or business for the three-year period ending with the close of the taxable year preceding the declaration of a dividend, then a portion of any dividend paid by the foreign corporation to its shareholders will be treated as U.S.-source and, in the case of dividends paid to foreign shareholders, will be subject to withholding tax. This rule is sometimes referred to as the "secondary withholding tax."		
10. Provide equal treatment for interest paid by foreign partnerships and foreign corporations (sec. 310 of the House bill and sec. 228 of the Senate amendment)	Interest income from obligations of noncorporate U.S. residents or domestic corporations generally is treated as U.S.-source income. Other interest (e.g., interest on obligations of foreign corporations and foreign partnerships) generally is treated as foreign-source income.	Treats interest paid by foreign partnerships in a manner similar to the treatment of interest paid by foreign corporations. Thus, interest paid by a foreign partnership is treated as U.S.-source income only if the interest is paid by a U.S. trade or business	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	However, Treasury regulations provide that a foreign partnership is a U.S. resident for purposes of this rule if at any time during its taxable year it is engaged in a trade or business in the United States. Therefore, any interest received from such a foreign partnership is U.S.-source income. Notwithstanding the general rule described above, in the case of a foreign corporation engaged in a U.S. trade or business (or having gross income that is treated as effectively connected with the conduct of a U.S. trade or business), interest paid by such U.S. trade or business is treated as if it were paid by a domestic corporation (i.e., such interest is treated as U.S.-source income).	conducted by the partnership or is allocable to income that is treated as effectively connected with the conduct of a U.S. trade or business. Applies only to foreign partnerships that are predominantly engaged in the active conduct of a trade or business outside the United States. Effective date.–Taxable years beginning after December 31, 2003.	
11. Look-through treatment of payments between related CFCs (sec. 311 of the House bill and sec. 222 of the Senate amendment)	In general, the rules of subpart F require U.S. shareholders with a 10-percent or greater interest in a controlled foreign corporation ("CFC") to include certain income of the controlled foreign corporation (referred to as "subpart F income") on a current basis for U.S. tax purposes, regardless of	Dividends, interest, rents, and royalties received by one controlled foreign corporation from a related controlled foreign corporation are not treated as foreign personal holding company income to the extent attributable to non-subpart-F earnings of the payor.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	whether the income is distributed to the shareholders. Subpart F income includes foreign base company income. One category of foreign base company income is foreign personal holding company income. For subpart F purposes, foreign personal holding company income generally includes dividends, interest, rents and royalties, among other types of income. However, foreign personal holding company income does not include dividends and interest received by a controlled foreign corporation from a related corporation organized and operating in the same foreign country in which the controlled foreign corporation is organized, or rents and royalties received by a controlled foreign corporation from a related corporation for the use of property within the country in which the controlled foreign corporation is organized. Interest, rent, and royalty payments do not qualify for this exclusion to the extent that such payments reduce the subpart F income of the payor.	For these purposes, a related controlled foreign corporation is a controlled foreign corporation that controls or is controlled by the other controlled foreign corporation, or a controlled foreign corporation that is controlled by the same person or persons that control the other controlled foreign corporation. Ownership of more than 50 percent of the controlled foreign corporation's stock (by vote or value) constitutes control for these purposes. Effective date.–Taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders with or within which such taxable years of such foreign corporations end.	

Provision	Present Law	House Bill	Senate Amendment
12. Look-through treatment under subpart F for sales of partnership interests (sec. 312 of the House bill and sec. 223 of the Senate amendment)	If a controlled foreign corporation sells a partnership interest at a gain, the gain generally constitutes foreign personal holding company income and is included in the income of 10-percent U.S. shareholders of the controlled foreign corporation as subpart F income.	Treats the sale by a controlled foreign corporation of a partnership interest as a sale of the proportionate share of partnership assets attributable to such interest for purposes of determining subpart F foreign personal holding company income. This rule applies only to partners owning directly, indirectly, or constructively at least 25 percent of a capital or profits interest in the partnership. Thus, the sale of a partnership interest by a controlled foreign corporation that meets this ownership threshold constitutes subpart F income under the proposal only to the extent that a proportionate sale of the underlying partnership assets attributable to the partnership interest would constitute subpart F income. Effective date.–Taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders with or within which such taxable years of such foreign corporations end.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
13. Repeal of foreign personal holding company rules and foreign investment company rules (sec. 313 of the House bill and sec. 211 of the Senate amendment)	Income earned by a foreign corporation from its foreign operations generally is subject to U.S. tax only when such income is distributed to a U.S. person that holds stock in such corporation. The Code sets forth the following anti-deferral rules which impose current U.S. tax or interest charges on certain income earned by a U.S. person through a foreign corporation: • the controlled foreign corporation rules of subpart F (secs. 951-964); • the passive foreign investment company rules (secs. 1291-1298); • the foreign personal holding company rules (secs. 551-558); • the personal holding company rules (secs. 541-547); • the accumulated earnings tax rules (secs. 531-537); and • the foreign investment company rules (secs. 1246-1247).	The provision reduces the complexity that results from overlap among the various anti-deferral regimes by: (1) eliminating the rules applicable to foreign personal holding companies and foreign investment companies; (2) excluding foreign corporations from the application of the personal holding company rules; and (3) including as subpart F foreign personal holding company income personal services contract income that is subject to the present-law foreign personal holding company rules. <u>Effective date</u>.–The provision is effective for taxable years beginning after December 31, 2004, and taxable years of U.S. shareholders with or within such taxable years of such foreign corporations end.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
14. Determination of foreign personal holding company income with respect to transactions in commodities (sec. 314 of the House bill and sec. 206 of the Senate amendment)	Under the subpart F rules, U.S. shareholders with a 10-percent or greater interest in a controlled foreign corporation ("U.S. 10-percent shareholders") are subject to U.S. tax currently on certain income earned by the controlled foreign corporation, whether or not such income is distributed to the shareholders. The income subject to current inclusion under the subpart F rules includes, among other things, "foreign personal holding company income." With respect to transactions in commodities, foreign personal holding company income does not consist of gains or losses which arise out of bona fide hedging transactions that are reasonably necessary to the conduct of any business by a producer, processor, merchant, or handler of a commodity in the manner in which such business is customarily and usually conducted by others. In addition, foreign personal holding company income does not consist of gains or losses which are comprised of active business gains or losses from the sale of commodities, but only if	Modifies the requirements that must be satisfied for gains or losses from a commodities hedging transaction to qualify for exclusion from the definition of subpart F foreign personal holding company income. Under the provision, gains or losses from a transaction with respect to a commodity are not treated as foreign personal holding company income if the transaction satisfies the general definition of a hedging transaction under the Code, as modified for this purpose. Also changes the requirements that must be satisfied for active business gains or losses from the sale of commodities to qualify for exclusion from the definition of foreign personal holding company income. Under the provision, such gains or losses are not treated as foreign personal holding company income if substantially all of the controlled foreign corporation's commodities are comprised of: (1) stock in trade, inventory, or property held primarily for sale to customers in the ordinary course of trade or business; (2) depreciable trade or business property; or (3) supplies.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	substantially all of the controlled foreign corporation's business is as an active producer, processor, merchant, or handler of commodities.	Also provides that, for purposes of applying the requirements for active business gains or losses from commodities sales to qualify for exclusion from the definition of foreign personal holding company income, commodities with respect to which gains or losses are not taken into account as foreign personal holding company income by a regular dealer in commodities (or financial instruments referenced to commodities) are not taken into account in determining whether substantially all of the dealer's commodities are comprised of the property described above. Effective date.–Transactions entered into after December 31, 2004.	
15. Active leasing income from aircraft and vessels (sec. 315 of the House bill and sec. 221 of the Senate amendment)	In general, the subpart F rules require U.S. shareholders with a 10-percent or greater interest in a controlled foreign corporation ("CFC") to include currently in income for U.S. tax purposes certain income of the CFC (referred to as "subpart F income"), without regard to whether the income is distributed to the	Repeals the subpart F rules relating to foreign base company shipping income. Also amends the exception from foreign personal holding company income applicable to rents or royalties derived from unrelated persons in the active conduct of a trade or business, by providing a safe harbor for rents derived from	Provides that "qualified leasing income" derived from or in connection with the leasing or rental of any aircraft or vessel is not treated as foreign personal holding company income or foreign base company shipping income. Also, defines "qualified leasing income" as rents or gains derived in the active conduct of a

Provision	Present Law	House Bill	Senate Amendment
	shareholders. Subpart F income includes foreign base company shipping income and foreign personal holding company income. Foreign base company shipping income generally includes income derived from the use of an aircraft or vessel in foreign commerce, the performance of services directly related to the use of any such aircraft or vessel, the sale or other disposition of any such aircraft or vessel, and certain space or ocean activities. Foreign commerce generally involves the transportation of property or passengers between a port (or airport) in the U.S. and a port (or airport) in a foreign country, two ports (or airports) within the same foreign country, or two ports (or airports) in different foreign countries. Foreign personal holding company income generally includes rents and royalties, except rents and royalties received by a CFC in the active conduct of a trade or business from unrelated persons as determined under a facts and circumstances test. Treasury regulations provide that rents are	leasing an aircraft or vessel in foreign commerce. Such rents are excluded from foreign personal holding company income if the active leasing expenses comprise at least 10 percent of the profit on the lease. The safe harbor will not prevent a lessor from otherwise showing it actively carries on a trade or business. Such a showing can be made if a lessor regularly and directly performs active and substantial marketing, remarketing, management and operational functions with respect to the leasing of an aircraft or vessel (or component engines). An aircraft or vessel is considered to be leased in foreign commerce if it is used for the transportation of property or passengers between a port or airport in the United States and one in a foreign country or between foreign ports or airports, provided the aircraft or vessel is used predominantly outside the United States. An aircraft or vessel will be considered used predominately outside the United States if more than 50 percent of its miles traveled during the taxable	leasing trade or business with respect to which the CFC conducts substantial activity, provided that the leased property is used by the lessee or other end-user in foreign commerce and predominantly outside the United States, and such lessee or other end-user is not related to the CFC. The determination of whether an aircraft or vessel is leased in foreign commerce is the same as under the House bill, except the United States includes U.S. possessions for this purpose. The determination of whether an aircraft or vessel is used predominantly outside the United States is the same as under the House bill, except 70 percent is substituted for 50 percent.

Provision	Present Law	House Bill	Senate Amendment
	treated as derived in the active conduct of a trade or business if they are derived from property that is leased as a result of the performance of marketing functions by the lessor if the lessor (through its own officers or employees located in a foreign country) maintains and operates an organization in such country that regularly engages in the business of marketing, or marketing and servicing, the leased property and that is substantial in relation to the amount of rents derived from the leasing of such property. An organization in a foreign country is substantial in relation to rents if the active leasing expenses equal at least 25 percent of the adjusted leasing profit.	year are traveled outside the United States or the aircraft or vessel is located outside the United States more than 50 percent of the time during the taxable year. Effective date.–Effective for taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders with or within which such taxable years of foreign corporations end.	Effective date.–Effective for taxable years of foreign corporations beginning after December 31, 2005, and taxable years of U.S. shareholders with or within which such taxable years of such foreign corporations end.
16. Modification of subpart F exemption for active financing (sec. 316 of the House bill and sec. 226 of the Senate amendment)	Under the subpart F rules, U.S. shareholders with a 10-percent or greater interest in a controlled foreign corporation ("CFC") are subject to U.S. tax currently on certain income earned by the CFC, whether or not such income is distributed to the shareholders. The income subject to current inclusion under the subpart F rules includes, among other things, foreign base	Modifies the temporary exceptions from subpart F foreign personal holding company income and foreign base company services income for income derived in the active conduct of a banking, financing, or similar business. For purposes of determining whether a CFC or QBU has conducted directly in its home country substantially all of the activities in	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	company service income, foreign personal holding company income, and insurance income. Temporary exceptions from foreign personal holding company income, foreign base company services income, and insurance income apply for subpart F purposes for certain income that is derived in the active conduct of a banking, financing, or similar business, or in the conduct of an insurance business ("active financing income"). With respect to income derived in the active conduct of a banking, financing, or similar business, a CFC is required to be predominantly engaged in such business and to conduct substantial activity with respect to such business in order to qualify for the exceptions. In addition, income derived by a CFC or a qualified business unit ("QBU") of a CFC from transactions with customers is eligible for the exceptions if, among other things, substantially all of the activities in connection with such transactions are conducted directly by the CFC or QBU in its home country.	connection with transactions with customers, provides that an activity is treated as conducted directly by the CFC or QBU in its home country if the activity is performed by employees of a related person and: (1) the related person is itself an eligible CFC the home country of which is the same as that of the CFC or QBU; (2) the activity is performed in the home country of the related person; and (3) the related person is compensated on an arm's length basis for the performance of the activity by its employees and such compensation is treated as earned by such person in its home country for purposes of the tax laws of such country. For purposes of determining whether a CFC or QBU is eligible to earn active financing income, such activity may not be taken into account by any CFC or QBU (including the employer of the employees performing the activity) other than the CFC or QBU for which the activities are performed. <u>Effective date</u>.–Taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders	

Provision	Present Law	House Bill	Senate Amendment
		with or within which such taxable years of foreign corporations end.	
17. 20-year foreign tax credit carryover; one-year foreign tax credit carryback (sec. 201 of the Senate amendment)	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 to the two immediately preceding taxable years (to the earliest year first) and carried forward five taxable years (in chronological order) and credited to the extent that the taxpayer otherwise has excess foreign tax credit limitation for those years. Excess credits are carried forward or carried back on a separate limitation basis. Thus, if a taxpayer has excess foreign tax credits in one separate limitation category for a taxable year, those excess credits may be carried back and forward only as taxes allocable to that category, notwithstanding the fact that the taxpayer may have excess foreign tax credit limitation in another category for that year. If credits cannot be so utilized, they are permanently disallowed.	No provision.	The Senate amendment extends the excess foreign tax credit carryforward period to twenty years and limits the carryback period to one year. Effective date.–The extension of the carryforward period is effective for excess foreign tax credits that may be carried to any taxable years ending after the date of enactment of the provision; the limited carryback period is effective for excess foreign tax credits arising in taxable years beginning after the date of enactment of the provision.

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18. Expand the subpart F de minimis rule to the lesser of five percent of gross income or $5 million (sec. 212 of the Senate amendment)	Under the rules of subpart F, U.S. 10-percent shareholders of a controlled foreign corporation are required to include in income currently for U.S. tax purposes certain types of income of the controlled foreign corporation, whether or not such income is actually distributed currently to the shareholders (referred to as "subpart F income"). Subpart F income includes foreign base company income and certain insurance income. Foreign base company income includes five categories of income: foreign personal holding company income, foreign base company sales income, foreign base company services income, foreign base company shipping income, and foreign base company oil-related income. Under a de minimis rule, if the gross amount of a controlled foreign corporation's foreign base company income and insurance income for a taxable year is less than the lesser of five percent of the controlled foreign corporation's gross income or $1 million, then no	No provision.	The Senate amendment expands the subpart F de minimis rule to provide that, if the gross amount of a controlled foreign corporation's foreign base company income and insurance income for a taxable year is less than the lesser of five percent of the controlled foreign corporation's gross income or $5 million, then no part of the controlled foreign corporation's gross income is treated as foreign base company income or insurance income. <u>Effective date</u>.–Taxable years of foreign corporations beginning after December 31, 2004, and taxable years of U.S. shareholders with or within which such taxable years of such foreign corporations end.

Provision	Present Law	House Bill	Senate Amendment
	part of the controlled foreign corporation's gross income is treated as foreign base company income or insurance income.		
19. Limit application of uniform capitalization rules in the case of foreign persons (sec. 214 of the Senate amendment)	Taxpayers generally may not currently deduct the costs incurred in producing property or acquiring property for resale. In general, the uniform capitalization rules require that a portion of the direct and indirect costs of producing property or acquiring property for resale be capitalized or included in the cost of inventory. The uniform capitalization rules apply to foreign corporations, whether or not engaged in business in the United States. In the case of a foreign corporation not engaged in a trade or business in the United States, the corporation’s taxable income and earnings and profits may nonetheless be relevant under the Code. For example, the subpart F income of a controlled foreign corporation may be currently includible on the return of a U.S. shareholder of the controlled foreign corporation.	No provision.	The Senate amendment provides that, in lieu of the uniform capitalization rules, costs incurred in producing property or acquiring property for resale are capitalized using U.S. generally accepted accounting principles (i.e., the method used to ascertain income, profit, or loss for purposes of reports or statements to shareholders, partners, other proprietors, or beneficiaries, or for credit purposes) for purposes of determining a U.S.-owned foreign corporation’s earnings and profits and subpart F income. The uniform capitalization rules continue to apply to foreign corporations for purposes of determining income effectively connected with a U.S. trade or business and the related earnings and profits therefrom. <u>Effective date</u>.–Taxable years beginning after December 31, 2004.

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20. Eliminate 30-percent tax on certain U.S.-source capital gains of nonresident individuals (sec. 216 of the Senate amendment)	Under the special capital gains tax of section 871(a)(2), a nonresident individual who is physically present in the United States for 183 days or more during a taxable year is subject to a 30-percent tax on the excess of U.S.-source capital gains over U.S.-source capital losses.	No provision.	The provision repeals the special tax on certain capital gains of nonresident aliens under section 871(a)(2). Effective date.–Taxable years beginning after December 31, 2003.
21. Modification of the treatment of certain REIT distributions attributable to gain from sales or exchanges of U.S. real property interests (sec. 230 of the Senate amendment)	The Foreign Investors in Real Property Tax Act ("FIRPTA") requires foreign investors to treat certain otherwise nontaxable capital gain from the sale of U.S. real property as though such gain were effectively connected with a U.S. trade or business. The receipt of a distribution from a real estate investment trust ("REIT") is so treated to the extent attributable to the disposition of a U.S. real property interest by the REIT. Such distributions are generally subject to a withholding tax at a rate of 35 percent (or lower treaty rate). The recipients of such distributions are required to file a U.S. tax return. A foreign recipient that is a corporation may also be subject to a branch profits tax at a 30 percent or lower treaty rate.	No provision.	A REIT distribution to a foreign investor of the REIT capital gain from dispositions of U.S. real property interests is no longer treated as though such gain were effectively connected with a U.S. trade or business, provided that 1) the distribution is received with respect to a class of stock that is regularly traded on an established securities market located in the U.S. and 2) the foreign investor does not own more than 5 percent of the class of stock at any time during the taxable year. The foreign investor is not required to file a U.S. Federal income tax return by reason of receiving such a distribution; and the distribution is treated as a dividend to that investor. The branch profits tax

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			also no longer applies to such a distribution. Effective date.–Taxable years beginning after the date of enactment.
22. Exclusion of certain horse-racing and dog-racing gambling winnings from the income of nonresident alien individuals (sec. 232 of the Senate amendment)	Certain items of gross income received by a nonresident alien from sources within the United States are subject to a flat 30-percent withholding tax. Gambling winnings received by a nonresident alien from wagers placed in the United States are U.S.-source and thus generally are subject to this withholding tax, unless specifically exempted by statute or treaty. With respect to gambling winnings of a nonresident alien resulting from a wager initiated outside the United States on a pari-mutuel event taking place within the United States, the source of the winnings, and thus the applicability of the 30-percent U.S. withholding tax, depends on the type of wagering pool from which the winnings are paid. If the payout is made from a separate foreign pool, maintained	No provision.	The Senate amendment provides an exclusion from gross income for winnings paid to a nonresident alien resulting from a legal wager initiated outside the United States in a pari-mutuel pool on a live horse or dog race in the United States, regardless of whether the pool is a separate foreign pool or a merged U.S.-foreign pool. Effective date.–Wagers made after date of enactment.

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	completely in a foreign jurisdiction (e.g., a pool maintained by a racetrack or off-track betting parlor that is showing in a foreign country a simulcast of a horse race taking place in the United States), then the winnings paid to a nonresident alien generally would not be subject to withholding tax, because the amounts received generally would not be from sources within the United States. However, if the payout is made from a "merged" or "commingled" pool, in which betting pools in the United States and the foreign country are combined for a particular event, then the portion of the payout attributable to wagers placed in the United States could be subject to withholding tax.		
23. Limitation of withholding on U.S.-source dividends paid to Puerto Rico corporations (sec. 233 of the Senate amendment)	In general, dividends paid by corporations organized in the United States (which does not include possessions) to corporations organized outside of the United States and its possessions, or to Puerto Rico corporations, are subject to U.S. income tax withholding at the flat rate of 30 percent. Corporations organized in the U.S. possessions	No provision.	Lowers the withholding income tax rate on U.S. source dividends paid to a corporation created or organized in Puerto Rico from 30 percent to 10 percent, to create parity with the 10 percent withholding tax imposed by Puerto Rico on dividends paid to non-Puerto Rico corporations. The lower rate applies only if the same local ownership and activity

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	of the Virgin Islands, Guam, American Samoa or the Northern Mariana Islands are not subject to withholding tax on dividends from corporations organized in the United States, provided that certain local ownership and activity requirements are met. Under the tax laws of Puerto Rico, a 10-percent withholding tax is imposed on dividends paid by Puerto Rico corporations to non-Puerto Rico corporations.		requirements are met that are applicable to corporations organized in other possessions receiving dividends from corporations organized in the United States. Effective date.–Dividends paid after date of enactment.
24. Report on WTO dispute settlement panels and the appellate body (sec. 234 of the Senate amendment)	The World Trade Organization ("WTO") is the only global international organization dealing with the rules of trade between nations, as agreed to by the member countries in trade agreements. The WTO is not only involved in the forming of such rules but it is also involved in the settlement of trade disputes that arise between member nations.	No provision.	Requires that by no later than March 31, 2004, the Secretary of Commerce, in consultation with the United States Trade Representative, shall transmit a report to the Senate Committee on Finance and the House of Representatives Committee on Ways and Means regarding whether dispute settlement panels or the Appellate Body of the World Trade Organization have: (1) added to or diminished the rights of the United States by imposing obligations and restrictions on the use of antidumping, countervailing, or safeguard measures not agreed to

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			under the World Trade Organization Antidumping Agreement, the Agreement on Subsidies and Countervailing Measures, or the Agreement on Safeguards; (2) appropriately applied the standard of review contained in Article 17.6 of the Antidumping Agreement; or (3) exceeded its authority or terms of reference. Effective date.–The provision is effective on the date of enactment.
25. Study of impact of international tax laws on taxpayers other than large corporations (sec. 235 of the Senate amendment)	The United States employs a "worldwide" tax system, under which U.S. persons (including domestic corporations) generally are taxed on all income, whether derived in the United States or abroad. In contrast, foreign persons (including foreign corporations) are subject to U.S. tax only on U.S.-source income and income that has a sufficient nexus to the United States. The United States generally provides a credit to U.S. persons for foreign income taxes paid or accrued. The	No provision.	The provision requires the Secretary of the Treasury or a delegate to conduct a study of the impact of Federal international tax rules on taxpayers other than large corporations, including the burdens placed on such taxpayers in complying with such rules. No later than 180 days after the date of the enactment of this provision, the Secretary shall report to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives the results of the

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	foreign tax credit generally is limited to the U.S. tax liability on a taxpayer's foreign-source income.		study conducted as a result of this provision. Effective date.–The provision is effective on the date of enactment.
26. Delay in effective date of final regulations governing exclusion of income from international operation of ships and aircraft (sec. 236 of the Senate amendment)	Section 883 generally provides an exemption from gross income for earnings of a foreign corporation derived from the international operation of ships and aircraft if an equivalent exemption from tax is granted by the applicable foreign country to corporations organized in the United States. Treasury has issued regulations implementing the rules of section 883 that are effective for taxable years beginning 30 days or more after August 26, 2003. The regulations provide, in general, that a foreign corporation organized in a qualified foreign country and engaged in the international operation of ships or aircraft shall exclude qualified income from gross income for purposes of United States Federal income taxation, provided that the corporation can satisfy certain ownership and related documentation requirements. The	No provision.	Delays the effective date for the Treasury regulations so that they apply to taxable years of foreign corporations seeking qualified foreign corporation status beginning after December 31, 2004. Effective date.–The provision is effective after date of enactment.

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	proposed rules explain when a foreign country is a qualified foreign country and what income is considered to be qualified income.		
27. Interest payments deductible where taxpayer could have borrowed without a guarantee (sec. 237 of the Senate amendment)	Present law provides rules to limit the ability of U.S. corporations to reduce the U.S. tax on their U.S.-source income through earnings stripping transactions. These rules limit the deductibility of interest paid to certain related parties ("disqualified interest"), if the payor's debt-equity ratio exceeds 1.5 to 1 and the payor's net interest expense exceeds 50 percent of its "adjusted taxable income" (generally taxable income computed without regard to deductions for net interest expense, net operating losses, and depreciation, amortization, and depletion). Disqualified interest for these purposes also may include interest paid to unrelated parties in certain cases in which a related party guarantees the debt.	No provision.	A foreign related-party guarantee does not trigger the earnings stripping rules to the extent of the amount of debt that the taxpayer establishes (to the satisfaction of the Treasury Secretary) that it could have borrowed without the guarantee. <u>Effective date</u>.–Guarantees issued on or after date of enactment.