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

REVENUE PROVISIONS

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JOINT COMMITTEE ON TAXATION

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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 that raise revenue.

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 exclusions, domestic production, corporate income tax rates applicable to small corporations, tax incentives for manufacturers, small

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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: Revenue Provisions* (JCX-64-04), 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.

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
A. Provisions to Reduce Tax Avoidance Through Individual and Corporate Expatriation **1. Tax treatment of inverted corporate entities (sec. 601 of the House bill and sec. 441 of the Senate amendment)**	U.S. corporations may reincorporate in low-tax foreign jurisdictions and thereby replace the U.S. parent corporation of a multinational corporate group with a foreign parent corporation. This allows the corporate group to remove certain foreign operations from the U.S. taxing jurisdiction. The corporate group may derive further tax benefits from the inverted structure by reducing U.S. tax on U.S.-source income through various earnings stripping or other transactions. (*See, e.g.*, secs. 163(j) and 482). Inversion transactions may give rise to immediate U.S. tax consequences at the shareholder and/or the corporate level, depending on the type of inversion.	Special tax rules apply to corporations that undertake certain defined inversion transactions. A corporate inversion transaction is a transaction in which: (1) a U.S. corporation becomes a subsidiary of a foreign-incorporated entity after March 4, 2003; (2) the former shareholders of the U.S. corporation hold (by reason of holding stock in the U.S. corporation) 60 percent or more of the stock (by vote or value) of the foreign-incorporated entity after the transaction; and (3) the foreign-incorporated entity, considered together with all companies connected to it by a chain of greater than 50-percent ownership (the "expanded affiliated group"), does not conduct substantial business activities in the entity's country of incorporation, compared to the total worldwide	Defines two different types of corporate inversion transactions and establishes a different set of consequences for each type. The first type of inversion is a transaction in which: (1) a U.S. corporation becomes a subsidiary of a foreign-incorporated entity; (2) the former shareholders of the U.S. corporation hold 80 percent or more of the stock (by vote or value) of the foreign-incorporated entity after the transaction; and (3) the foreign-incorporated entity, considered together with all companies connected to it by a chain of greater than 50-percent ownership (the "expanded affiliated group"), does not have substantial business activities in the entity's country of incorporation, compared to the total worldwide business activities of the expanded affiliated group.

Provision	Present Law	House Bill	Senate Amendment
		business activities of the expanded affiliated group. Certain partnership transactions are also treated as inversion transactions. Any applicable corporate-level "toll charges" for establishing the inverted structure are not offset by tax attributes such as net operating losses or foreign tax credits. This rule does not apply to certain transfers of inventory and similar property. These measures generally apply for a 10-year period following the inversion transaction.	Deems the top-tier foreign corporation in such an inversion transaction to be a domestic corporation for all purposes of the Code. The second type of inversion transaction meets the definition above, except that the 80-percent ownership threshold is not met. In such a case, the inversion transaction is respected (i.e., the foreign corporation is treated as foreign), but: (1) any applicable corporate-level "toll charges" for establishing the inverted structure may not be offset by tax attributes such as net operating losses or foreign tax credits; (2) the accuracy-related penalty is increased; and (3) section 163(j), relating to "earnings stripping" through related-party debt, is strengthened. These measures generally apply for a 10-year period following the inversion transaction.

Provision	Present Law	House Bill	Senate Amendment
		Effective date.–The provision applies to taxable years ending after March 4, 2003.	Effective date.–Regime applicable to transactions involving at least 80 percent identity of ownership applies to inversion transactions completed after March 20, 2002. Rules for inversion transactions involving greater-than-50-percent identity of ownership apply to inversion transactions completed after 1996 that meet the 50-percent test and to inversion transactions completed after 1996 that would have met the 80-percent test but for the March 20, 2002, date.
2. Excise tax on stock compensation of insiders in inverted corporations (sec. 602 of the House bill and sec. 443 of the Senate amendment)	While shareholders are generally required to recognize gain upon stock inversion transactions, an inversion transaction is generally not a taxable event for holders of stock options and other stock-based compensation.	Upon certain inversion transactions, imposes an excise tax on certain executives (including executives of the expanded affiliated group) holding stock options and other stock-based compensation equal to 15 percent of the value of the specified stock compensation. Effective date.–Generally effective March 4, 2003.	Similar to the House bill, except that the excise tax is equal to 20 percent of the value of the specified stock compensation and the excise tax does not apply to executives of the expanded affiliated group. Effective date.–Generally effective July 11, 2002.

Provision	Present Law	House Bill	Senate Amendment
3. Reinsurance agreements (sec. 603 of the House bill and sec. 444 of the Senate amendment)	In the case of a reinsurance agreement between two or more related persons, the Treasury Secretary has authority to allocate among the parties or recharacterize income (whether investment income, premium or otherwise), deductions, assets, reserves, credits and any other items related to the reinsurance agreement, or make any other adjustment, in order to reflect the proper source and character of the items for each party.	Clarifies the rules giving Treasury the authority to allocate items among the parties to a reinsurance agreement, recharacterize items, or make any other adjustment, in order to reflect the proper source, character or amount of the items for each party. Effective date.–Any risk reinsured after date of enactment.	Same as the House bill except for effective date. Effective date.–Any risk reinsured after April 11, 2002.
4. Revision of tax rules on expatriation of individuals (sec. 604 of the House bill and sec. 442 of the Senate amendment)	In general, an individual who relinquishes U.S. citizenship or terminates U.S. residency with a principal purpose of avoiding U.S. taxes is subject to an alternative tax regime for income tax purposes for the 10 taxable years ending after expatriation or residency termination. Special rules apply to such individuals for estate and gift tax purposes. A special immigration rule denies certain former citizens re-entry into the United States if the Attorney General determines that their expatriation was tax-motivated.	Modifies present-law rules by providing: (1) objective standards for determining whether former citizens or former long-term residents are subject to the alternative tax regime; (2) tax-based (instead of immigration-based) rules for determining when an individual is no longer a U.S. citizen or long-term resident for U.S. Federal tax purposes; (3) the imposition of full U.S. taxation for individuals who are	The provision replaces the present-law income tax rules of the alternative tax regime with rules that generally: (1) subject certain U.S. citizens who relinquish their U.S. citizenship and certain long-term U.S. residents who terminate their U.S. residence to a mark-to-market regime with respect to all their property interests; (2) limit the net gain recognized on the deemed sale to the gain that exceeds $600,000 or $1.2 million (indexed) for a joint return; and

Provision	Present Law	House Bill	Senate Amendment
		subject to the alternative tax regime and who return to the United States for extended periods; (4) imposition of U.S. gift tax on gifts of stock of certain closely-held foreign corporations that hold U.S.-situated property; and (5) an annual return-filing requirement for individuals who are subject to the alternative tax regime, for each of the 10 years following citizenship relinquishment or residency termination. Effective date.–Applies to individuals who relinquish citizenship or terminate long-term residency after June 3, 2004.	(3) coordinate the present-law alternative tax regime and the mark-to-market regime such that the alternative tax regime generally does not apply to a former citizen or former long-term resident whose expatriation or residency termination occurs on or after January 1, 2004. A U.S. taxpayer who receives a gift or inheritance from an expatriate generally is required to include the value of such gift or inheritance in gross income and is subject to U.S. income tax on such amount. The provision denies former citizens reentry into the United States if the individual is determined not to be in compliance with his or her tax obligations under the provision (regardless of the subjective motive for expatriating). Effective date.–Applies to individuals who relinquish citizenship or terminate long-term residency after January 1, 2004.

Provision	Present Law	House Bill	Senate Amendment
5. Reporting of taxable mergers and acquisitions (sec. 605 of the House bill and sec. 445 of the Senate amendment)	Brokers (defined to include stock transfer agents) are required to make information returns and to provide corresponding payee statements as to sales made on behalf of their customers, subject to the penalty provisions of sections 6721-6724. This requirement generally does not apply with respect to taxable transactions other than exchanges for cash (e.g., stock inversion transactions taxable to shareholders by reason of section 367(a)).	If gain or loss is recognized in whole or in part by shareholders of a corporation by reason of a second corporation's acquisition of the stock or assets of the first corporation, then the acquiring corporation (or the acquired corporation, if so prescribed by the Secretary) is required to make a return containing certain information. Alternatively, a stock transfer agent who records transfers of stock in such transaction may make the return described above in lieu of the second corporation. Also, every person required to make a return described above is required to furnish to each shareholder (or the shareholder's nominee) whose name is required to be set forth in such return a written statement showing certain information. The present-law penalties for failure to comply with information reporting requirements are extended to failures to comply with	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
		the requirements set forth under this bill. Effective date.–Acquisitions after the date of enactment.	
6. Studies (sec. 606 of the House bill)	Due to the variation in tax rates and tax systems among countries, a multinational enterprise (U.S.-based or foreign-based) may have an incentive to shift income, deductions, or tax credits between group members in order to arrive at a reduced overall tax burden. Under section 482, the Treasury Secretary is authorized to reallocate income, deductions, or credits between or among two or more organizations, trades, or businesses under common control if she determines that such a reallocation is necessary to prevent tax evasion or to clearly reflect income. In addition to the statutory rules governing the taxation of foreign income of U.S. persons and U.S. income of foreign persons, bilateral income tax treaties limit the amount of income tax that may be imposed by one treaty partner on residents of the other treaty partner.	Requires the Treasury Secretary to conduct and submit to the Congress three studies. The first study will examine the effectiveness of the transfer pricing rules of section 482, with an emphasis on transactions involving intangible property. The second study will examine income tax treaties to which the United States is a party, with a view toward identifying any inappropriate reductions in withholding tax or opportunities for abuse that may exist. The third study will examine the impact of the provisions of this bill on inversion transactions. Effective date.–The tax treaty study required under the provision is due no later than June 30, 2005. The transfer pricing study required under the provision is due no later than June 30, 2005. The inversions study required under the provision is due no later than December 31,	No provision.

Provision	Present Law	House Bill	Senate Amendment
	For example, treaties often reduce or eliminate withholding taxes imposed by a treaty country on certain types of income (e.g., dividends, interest and royalties) paid to residents of the other treaty country.	2005.	
B. Tax Shelter Provisions **1. Provisions relating to reportable transactions and tax shelters** **(a) Penalty for failing to disclose reportable transaction (sec. 611 of House bill and sec. 402 of the Senate amendment)**	Although Treasury regulations require a taxpayer to disclose with its tax return certain information with respect to each "reportable transaction" in which the taxpayer participates, there is no specific penalty for failing to disclose a reportable transaction.	Creates a new $50,000 penalty ($10,000 in the case of a natural person) for any person who fails to disclose a reportable transaction. The amount is increased to $200,000 ($100,000 in the case of a natural person) if the failure is with respect to a listed transaction. The penalty with respect to a transaction (other than a listed transaction) can be waived by the Commissioner if the waiver would promote compliance and effective tax administration. <u>Effective date</u>.–Returns and statements the due date for which is after the date of enactment.	Same as the House bill, except the penalty amounts are: (1) $50,000 penalty for any person who fails to disclose a reportable transaction; (2) $100,000 if the failure is with respect to a listed transaction; and (3) doubled for large entities and high net worth individuals. Penalty waiver is same as House bill, except imposes additional conditions, including limited delegation of waiver authority by the Commissioner. Also requires a publicly traded entity that is required to pay a penalty for failing to disclose a listed transaction to disclose the imposition of the penalty in reports to the SEC. Also requires the Secretary to make public the name of any person required to pay such

Provision	Present Law	House Bill	Senate Amendment
			penalty and the amount of such penalty.
(b) Accuracy-related penalty for listed transactions and other reportable transactions having a significant tax avoidance purpose (sec. 612 of the House bill and sec. 403 of the Senate amendment)	In general, a 20-percent accuracy-related penalty applies to the portion of any underpayment that is attributable to (1) negligence, (2) any substantial understatement of income tax, (3) any substantial valuation misstatement, (4) any substantial overstatement of pension liabilities, or (5) any substantial estate or gift tax valuation understatement. Except in the case of tax shelters (as defined), the penalty is not applicable if substantial authority for the tax treatment exists or if the tax treatment is disclosed and reasonable basis for such treatment exists. In the case of non-corporate tax shelters, the penalty is not applicable if substantial authority for the tax treatment exists and the taxpayer reasonably believed that such treatment was more likely than not proper.	Provides a new accuracy-related penalty that applies to listed transactions and reportable transactions with a significant tax avoidance purpose ("reportable avoidance transactions"). The penalty rate and defenses available to avoid the penalty vary depending on whether the transaction was adequately disclosed. The present-law penalty does not apply to the extent the new penalty applies. Repeals the exception from the present-law penalty for non-corporate tax shelters. <u>Effective date</u>.–Taxable years ending after the date of enactment.	Same as the House bill, except also repeals the special rules for tax shelters. Also provides special rules that limit the assertion and compromise of the penalty. Also requires a publicly traded entity that is required to pay a penalty for an understatement of tax with respect to certain undisclosed tax avoidance transactions to disclose the imposition of the penalty in reports to the SEC. Also requires the Secretary to make public the name of any person required to pay such penalty and the amount of such penalty.

Provision	Present Law	House Bill	Senate Amendment
(c) Tax shelter exception to confidentiality privileges relating to taxpayer communications (sec. 613 of the House bill and sec. 406 of the Senate amendment)	With respect to tax advice, the same common law protections of confidentiality that apply to a communication between a taxpayer and an attorney also apply to a communication between a taxpayer and a Federally authorized tax practitioner, except for communications regarding corporate tax shelters.	Expands the exception for corporate tax shelters to all tax shelters, whether entered into by corporations, individuals, partnerships, tax-exempt entities, or any other entity. <u>Effective date</u>.–Communications made on or after the date of enactment.	Same as the House bill.
(d) Statute of limitations for taxable years for which required listed transactions not reported (sec. 614 of the House bill and sec. 416 of the Senate amendment)	Taxes generally must be assessed within three years after the date a return is filed. If there has been a substantial omission of items of gross income that totals more than 25 percent of the amount of gross income shown on the return, the period during which an assessment must be made is extended to six years. Tax may be assessed at any time if the taxpayer files a false or fraudulent return with the intent to evade tax or if the taxpayer does not file a tax return at all.	Extends the statute of limitations with respect to a listed transaction if a taxpayer fails to include with a tax return any required information with respect to the transaction. The statute of limitations with respect to such a transaction will not expire before the date which is one year after the earlier of (1) the date on which the Treasury Secretary is furnished the required information, or (2) the date that a material advisor satisfies the list maintenance requirements with respect to a request by the Secretary. <u>Effective date</u>.–Taxable years with respect to which the period for assessing a deficiency did not expire before the date of enactment.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
(e) Disclosure of reportable transactions (secs. 615 and 616 of the House bill and secs. 407 and 408 of the Senate amendment)	An organizer of a tax shelter is required to register the shelter with the Treasury Secretary not later than the day on which the shelter is first offered for sale. The penalty for failing to timely register a tax shelter generally is the greater of one percent of the aggregate amount invested in the shelter or $500. However, if the tax shelter involves an arrangement offered to a corporation under conditions of confidentiality, the penalty generally is the greater of $10,000 or 50 percent of the fees payable to any promoter with respect to offerings prior to the date of late registration.	Repeals the rules with respect to registration of tax shelters and, instead, requires each material advisor with respect to any reportable transaction to timely file an information return with the Secretary. Also repeals the penalty for failure to register tax shelters and, instead, imposes a penalty on any material advisor who fails to file an information return with respect to a reportable transaction. <u>Effective date</u>.–The provision requiring disclosure of reportable transactions by material advisors applies to transactions with respect to which material aid, assistance or advice is provided after the date of enactment. The provision imposing a penalty for failing to disclose reportable transactions applies to returns the due date for which is after the date of enactment.	Same as the House bill, except defines material advisers more broadly to include insurers of reportable transactions.

Provision	Present Law	House Bill	Senate Amendment
(f) Investor lists and modification of penalty for failure to maintain lists of investors (secs. 615 and 617 of the House bill and secs. 407 and 409 of the Senate amendment)	Any organizer or seller of a potentially abusive tax shelter must maintain a list identifying each person who was sold an interest in any such tax shelter with respect to which registration was required. The penalty for failing to maintain a required list is $50 for each name omitted from the list (with a maximum penalty of $100,000 per year).	Modifies the penalty for failing to maintain the required list by making it a time-sensitive penalty. Thus, a material advisor who is required to maintain an investor list and who fails to make the list available upon written request by the Secretary within 20 business days after the request will be subject to a $10,000 per day penalty. Effective date.–Requests made after the date of enactment.	Same as the House bill, except defines material advisers more broadly to include insurers of reportable transactions. Also clarifies that the identity of any person on an investor list is not privileged, effective as if included in the Deficit Reduction Act of 1984.
(g) Penalty on promoters of tax shelters (sec. 618 of the House bill and sec. 415 of the Senate amendment)	In general, a $1,000 penalty is imposed on any person who organizes, assists in the organization of, or participates in the sale of an interest in any entity or plan or arrangement, if in connection with such activity the person knowingly makes or furnishes a false or fraudulent statement or a gross valuation overstatement regarding the securing of any tax benefit by reason of holding an interest in the entity or participating in the plan or arrangement.	Modifies the penalty amount to equal 50 percent of the gross income derived by the person from the activity for which the penalty is imposed. The enhanced penalty does not apply to a gross valuation overstatement. Effective date.–Activities after the date of enactment.	Same as the House bill, except (1) modifies the penalty amount to equal 100 percent of the gross income derived by the person from the activity for which the penalty is imposed, (2) calculates the penalty with respect to each instance of such activity, each instance in which income was derived by the person subject to the penalty, and each person who participated in such activity, (3) imposes joint and several liability upon all persons subject to the penalty for such activity, and (4) provides that the payment of such penalty or any amount to settle or avoid the

Provision	Present Law	House Bill	Senate Amendment
			imposition of such penalty is not deductible.
(h) Penalty for aiding and abetting the understatement of tax liability (sec. 419 of the Senate amendment)	Imposes a penalty on persons who aid, assist in, procure, or advise with respect to the preparation or presentation of any portion of a return or other document if the person (1) knows or has reason to believe that the return or other document will be used in connection with any material matter arising under the tax laws, and (2) knows that such portion would result in an understatement of the tax liability of another person. The amount of the penalty is $1,000 ($10,000 if the other person is a corporation) with respect to each such document, up to one penalty per other person per taxable period.	No provision.	Modifies the calculation of the penalty to apply to each instance of aid, assistance, procurement, or advice (in addition to each document), with no limitation on the number of penalties per other person per taxable period, except that the amount of the penalty cannot exceed 100 percent of the gross income derived from such aid, assistance, procurement, or advice. Also imposes joint and several liability upon all persons subject to the penalty for such activity, and provides that the payment of such penalty or any amount to settle or avoid the imposition of such penalty is not deductible. <u>Effective date</u>.–Activities after the date of enactment.

Provision	Present Law	House Bill	Senate Amendment
2. Modifications of substantial understatement penalty for nonreportable transactions (sec. 619 of the House bill and sec. 405 of the Senate amendment)	An accuracy-related penalty equal to 20 percent applies to any substantial understatement of tax.	Modifies the definition of "substantial" for corporate taxpayers so that a corporate taxpayer has a substantial understatement if the amount of the understatement for the taxable year exceeds the lesser of: (1) 10 percent of the tax required to be shown on the return for the taxable year (or, if greater, $10,000); or (2) $10 million. Effective date.–Taxable years beginning after date of enactment.	Same as the House bill, except also: (1) elevates the standard that a taxpayer must satisfy in order to reduce the amount of an understatement for undisclosed items; and (2) authorizes (but does not require) the Secretary to publish a list of positions for which it believes there is not substantial authority or reasonable belief that the tax treatment is more likely than not the proper treatment.
3. Modification of actions to enjoin certain conduct related to tax shelters and reportable transactions (sec. 620 of the House bill and sec. 410 of the Senate amendment)	The Secretary may commence civil actions to enjoin any person from promoting abusive tax shelters or aiding or abetting the understatement of tax liability.	Expands present-law authority so that injunctions also may be sought with respect to the requirements relating to the reporting of reportable transactions and the keeping of lists of investors by material advisors. Effective date.–Day after the date of enactment.	Same as the House bill, except also allows injunctions to be sought with respect to violations of Circular 230.
4. Penalty on failure to report foreign financial accounts (sec. 621 of the House bill and sec. 412 of the Senate amendment)	There is a civil penalty for persons who willfully fail to keep records and file reports when that person makes a transaction or maintains an account with a foreign financial entity. In addition, any person who willfully violates this reporting	Adds an additional civil penalty of up to $5,000 that may be imposed on any person who violates this reporting requirement (without regard to willfulness).	Same as House bill, except: (1) the maximum additional civil penalty for non-willful act is up to $10,000; and (2) also increases the maximum present-law penalty for willful behavior to the greater of $100,000 or 50 percent of the

Provision	Present Law	House Bill	Senate Amendment
	requirement is subject to a criminal penalty.	Effective date.–Failures to report occurring after the date of enactment.	amount of the transaction or account.
5. Regulation of individuals practicing before the Department of the Treasury (sec. 622 of the House bill and sec. 414 of the Senate amendment)	The Treasury Secretary is authorized to regulate the practice of representatives of persons before the Treasury Department. The Secretary also is authorized to suspend or disbar from practice before the Department a representative who is incompetent, disreputable, violates the rules regulating practice before the Department, or willfully and knowingly misleads or threatens the person being represented.	Makes two modifications to expand these sanctions: (1) expressly permits censure as a sanction and (2) permits the imposition of a monetary penalty as a sanction. Effective date.–Actions taken after the date of enactment.	Same as the House bill, except for technical drafting differences.
6. Treatment of stripped interests in bond and preferred stock funds, etc. (sec. 631 of the House bill and sec. 461 of the Senate amendment)	Special rules are provided with respect to debt instruments in which there has been a separation in ownership between the underlying debt instrument and any interest coupon that has not yet become payable. Similar rules apply to preferred stock in which there has been a separation in ownership between such stock and any dividend on such stock that has not become payable.	Authorizes the Treasury Department to promulgate regulations that, in appropriate cases, apply rules that are similar to the present-law rules for stripped bonds and stripped preferred stock to direct or indirect interests in an entity or account substantially all of the assets of which consist of bonds, preferred stock, or any combination thereof. Effective date.–Purchases and dispositions occurring after the date of enactment.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
7. Minimum holding period for foreign tax credit on withholding taxes on income other than dividends (sec. 632 of the House bill and sec. 456 of the Senate amendment)	In general, U.S. persons may credit foreign taxes against U.S. tax on foreign-source income. The amount of foreign tax credits that may 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 limitations are applied to specific categories of income. Present law generally denies a U.S. shareholder (other than a securities dealer) the foreign tax credits normally available with respect to a dividend from a corporation or a RIC if the shareholder has not held the stock for more than 15 days (within a 30-day testing period) in the case of common stock or more than 45 days (within a 90-day testing period) in the case of preferred stock. If a taxpayer is denied foreign tax credits because the applicable holding period is not satisfied, the taxpayer is entitled to a deduction for the foreign taxes for which the credit is disallowed.	Expands the present-law disallowance of foreign tax credits to include credits for gross-basis foreign withholding taxes with respect to any item of income or gain from property if the taxpayer who receives the income or gain has not held the property for more than 15 days (within a 30-day testing period), exclusive of foreign tax credits that are subject to the present-law disallowance with respect to dividends. Rules similar to the present-law disallowance for foreign tax credits with respect to dividends apply to foreign tax credits that are subject to the provision. In addition, the Treasury Department is authorized to issue regulations providing that the provision does not apply in appropriate cases. <u>Effective date</u>.–Amounts paid or accrued more than 30 days after the date of enactment.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
8. Partnership basis adjustments (sec. 633 of the House bill and sec. 469 of the Senate amendment)	If a partnership elects under section 754, adjustments to the basis of partnership property are made following a transfer of a partnership interest and following a distribution of partnership property. If a partner contributes property to the partnership, any items of partnership income, gain, loss and deduction with respect to the contributed property are allocated among partners to take into account any built-in gain or loss at the time of the contribution.	Partnership basis adjustments are required (not elective) for a transfer of a partnership interest when there is a substantial built-in loss in partnership property (basis exceeds value by more than $250,000). For transfers of interests in an electing investment partnership, a partner-level loss limitation applies in lieu of partnership basis adjustments. Partnership basis adjustments are required for a distribution of property when there is a substantial basis reduction in partnership property (a downward adjustment of more than $250,000). A built-in loss on contributed property may be taken into account only by the contributing partner and not by any other partner, including a partner purchasing the partnership interest from the contributing partner. <u>Effective date</u>.–Transfers, distributions and contributions after the date of enactment.	Partnership basis adjustments are required (not elective) in the event of a partnership distribution or a transfer of a partnership interest, except that the partnership basis adjustments remain elective in the case of the transfer of a partnership interest by reason of the partner's death. The special rule of section 732(d) (relating to determining a partner's basis in later-distributed property) is repealed. <u>Effective date</u>.–Generally transfers and distributions after the date of enactment.

Provision	Present Law	House Bill	Senate Amendment
9. No reduction of basis under section 734 in stock held by partnership in corporate partner (sec. 634 of the House bill and sec. 432 of the Senate amendment)	If a partnership elects under section 754, adjustments to the basis of partnership property are made following a transfer of a partnership interest and following a distribution of partnership property. The allocation of the increase or decrease in the basis of partnership property generally is made so as to reduce the difference between the value and the basis of the property.	A partnership is precluded from decreasing the basis of corporate stock of a partner or a related person, in applying the basis allocation rules following a distribution in liquidation of a partner's interest. Any decrease that would have been allocated to the stock is allocated to other partnership property, or, if the decrease exceeds the basis of that property, then gain is recognized by the partnership in the amount of the excess. <u>Effective date</u>.–Distributions after the date of enactment.	Same as the House bill, except for the effective date. <u>Effective date</u>.–Distributions after February 13, 2003.
10. Repeal of special rules for FASITs (sec. 635 of the House bill and sec. 433 of the Senate amendment)	<u>Financial asset securitization investment trusts (FASITs)</u>.–A FASIT is a non-taxable entity intended to facilitate the securitization of debt obligations such as credit card receivables, home equity loans, and auto loans. <u>Real estate mortgage investment conduits (REMICs)</u>.–A REMIC is a self-liquidating, non-taxable entity that holds a fixed pool of mortgages and issues multiple classes of investor interests. In	<u>FASITs</u>.–Repeals the special rules for FASITs, with a transition period for existing FASITs, pursuant to which the repeal of the FASIT rules would not apply to any FASIT in existence on the date of enactment to the extent that regular interests issued by the FASIT prior to such date continue to remain outstanding in accordance with their original terms.	Same as the House bill, except for the effective date.

Provision	Present Law	House Bill	Senate Amendment
	order to qualify as a REMIC, substantially all of the assets of the entity must consist of qualified mortgages and permitted investments as of the close of the third month beginning after the startup day of the entity.	REMICs.–Modifies the definitions of REMIC regular interests, qualified mortgages, and permitted investments so that reverse mortgage loans and government-originated loan pools can be transferred to, or purchased by, a REMIC. Effective date.–After February 13, 2003, except as provided by the transition period for existing FASITs.	Effective date.–After December 31, 2004, except as provided by the transition period for existing FASITs.
11. Limitation on transfer or importation of built-in losses (sec. 636 of the House bill and sec. 431 of the Senate amendment)	Generally, no gain or loss is recognized when one or more persons transfer property to a corporation in exchange for stock and immediately after the exchange such person or persons control the corporation. The transferor's basis in the stock of the controlled corporation is the same as the basis of the property contributed to the controlled corporation, increased by the amount of any gain (or dividend) recognized by the transferor on the exchange, and reduced by the amount of any money or property received, and by the amount of any loss recognized by the transferor.	Provides that if a residual interest in a REMIC is contributed to a corporation and the transferee corporation's adjusted basis in the REMIC residual interest exceeds the fair market value of the REMIC residual interest immediately after the contribution, the transferee corporation's adjusted basis in the REMIC residual interest is limited to the fair market value of the REMIC residual interest immediately after the contribution, regardless of whether the fair market value of the REMIC residual interest is less than, equal to, or greater than zero.	Importation of built-in losses.–Provides that if a net built-in loss is imported into the U.S in a tax-free organization, reorganization or liquidation from persons not subject to U.S. tax, the basis of each property so transferred is its fair market value. Limitation on transfer of built-in-losses in section 351 transactions.–Provides that if the aggregate adjusted bases of property contributed by a transferor (or by a control group of which the transferor is a member) to a corporation exceed the aggregate fair market value of the property transferred in a tax-free incorporation, the transferee's

Provision	Present Law	House Bill	Senate Amendment
	The basis of property received by a corporation, whether from domestic or foreign transferors, in a tax-free incorporation, reorganization, or liquidation of a subsidiary corporation is the same as the adjusted basis in the hands of the transferor, adjusted for any gain recognized by the transferor.	Effective date.–Transactions after date of enactment.	aggregate bases of the property is limited to the aggregate fair market value of the transferred property. In the case of a transfer after which the transferor owns at least 80 percent of the vote and value of the stock of the transferee corporation, any required basis reduction is made to the stock received by the transferor and not to the assets transferred. Effective date.–Transactions after December 31, 2003.
12. Clarification of banking business for purposes of determining investment of earnings in U.S. property (sec. 637 of the House bill and sec. 451 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 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	Limits the exception from the definition of U.S. property for deposits with persons carrying on the banking business to deposits with persons at least 80 percent of the gross income of which is derived in the active conduct of a banking business from unrelated persons. For purposes of this provision, the deposit recipient and persons related to the deposit recipient are treated as one person in applying the 80-percent test. Effective date.–Date of enactment.	Similar to House bill, except limits the exception to deposits with "financial services providers," defined as persons (and related parties) at least 80 percent of the income of which is specified financial services income derived from unrelated persons.

Provision	Present Law	House Bill	Senate Amendment
	U.S. property are provided for, including (among other things) deposits with persons carrying on the banking business. With regard to the exception for deposits with persons carrying on the banking business, an appeals court recently concluded that a U.S. subsidiary of a U.S. shareholder was "carrying on the banking business" even though its operations were limited to the administration of the private label credit card program of the U.S. shareholder. Therefore, the court held that a CFC of the U.S. shareholder could make deposits with the subsidiary (e.g., through the purchase of certificates of deposit) under this exception, and avoid taxation of the deposits as an investment in U.S. property.		
13. Alternative tax for certain small insurance companies and modification of exemption from tax (sec. 638 of the House bill and sec. 493 of the Senate amendment)	A property and casualty insurance company may elect to be taxed only on taxable investment income if its net written premiums or direct written premiums (whichever is greater) do not exceed $1.2 million. A property and casualty insurer is eligible for tax-exempt status if its gross receipts do not exceed $600,000, and premiums received	The $1.2 million ceiling on net written premiums or direct written premiums for purposes of the election to be taxed only on taxable investment income is increased to $1.89 million, and is indexed after 2004.	Generally, the same as the House bill, except that the $1.89 million ceiling is indexed after 2005; in addition, the 50-percent-of-gross-receipts test for tax-exempt status is increased to 60 percent.

Provision	Present Law	House Bill	Senate Amendment
	for the taxable year are greater than 50 percent of its gross receipts.	Effective date.–Taxable years beginning after December 31, 2003.	Effective date.–Taxable years beginning after December 31, 2004, with transition rule for companies in receivership or liquidation.
14. Denial of deduction for interest on underpayments attributable to nondisclosed tax avoidance transactions (sec. 639 of the House bill and sec. 417 of the Senate amendment)	Corporations generally may deduct interest paid or accrued within a taxable year on indebtedness, including interest on indebtedness to the Federal government attributable to an underpayment of tax.	Disallows any deduction for interest paid or accrued within a taxable year on any portion of an underpayment of tax that is attributable to an understatement arising from: (1) an undisclosed reportable avoidance transaction; or (2) an undisclosed listed transaction. Effective date.–Underpayments attributable to transactions entered into in taxable years beginning after the date of enactment.	Same as the House bill, except also disallows any deduction for interest paid or accrued within a taxable year on any portion of an underpayment of tax that is attributable to an understatement arising from a transaction that lacks economic substance.
15. Clarification of rules for payment of estimated tax for certain deemed asset sales (sec. 640 of the House bill and sec. 481 of the Senate amendment)	Section 338(a)(1) allows a buyer corporation to elect unilaterally to treat a qualified stock purchase of a target corporation as an asset purchase. Where the target is a subsidiary in an affiliated group, section 338(h)(10) allows the buyer and seller corporation to elect jointly to treat a stock sale of the target as an asset sale.	Clarifies section 338(h)(13) to provide that the exception for estimated tax purposes does not apply with respect to a qualified stock purchase for which an election is made under section 338(h)(10). Effective date.–Transactions that occur after the date of enactment.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	Section 338(h)(13) provides that for purposes of estimated tax penalties, tax attributable to a deemed asset sale under section 338(a)(1) shall not be taken into account.		
16. Exclusion of like-kind exchange property from nonrecognition treatment on the sale or exchange of a principal residence (sec. 641 of the House bill and sec. 492 of the Senate amendment)	A taxpayer may exclude up to $250,000 ($500,000 if married filing a joint return) of gain realized on the sale or exchange of a principal residence. There are no special rules relating to the sale or exchange of a principal residence that was acquired in a like-kind exchange within the prior five years.	Provides that the exclusion for gain on the sale or exchange of a principal residence does not apply if the principal residence was acquired in a like-kind exchange in which any gain was not recognized within the prior five years. <u>Effective date</u>.–Sales or exchanges of principal residences after the date of enactment.	Same as the House bill.
17. Prevention of mismatching of interest and original issue discount deductions and income inclusions in transactions with related foreign persons (sec. 642 of the House bill and sec. 453 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 any U.S. person that holds stock in such corporation. However, certain anti-deferral regimes may cause the U.S. person to be taxed on a current basis in the United States on certain income earned by certain foreign corporations. The main anti-deferral regimes are the controlled foreign corporation ("CFC") rules	Provides that deductions for amounts accrued but unpaid (whether by U.S. or foreign persons) to related FPHCs, CFCs, or PFICs are allowable only to the extent that the amounts accrued by the payor are, for U.S. tax purposes, currently includible in the income of the direct or indirect U.S. owners of the related foreign corporation under the relevant inclusion rules. Deductions that have accrued but are not allowable	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	of subpart F, the passive foreign investment company ("PFIC") rules, and the foreign personal holding company ("FPHC") rules. As a general rule, there is allowed as a deduction all interest paid or accrued within the taxable year with respect to indebtedness, including the aggregate daily portions of original issue discount ("OID") of the issuer for the days during such taxable year. If a debt instrument is held by a related foreign person, however, any portion of such OID is not allowable as a deduction by the payor of such instrument until paid (the "related-foreign-person rule"). Treasury regulations apply the related-foreign-person rule to the deduction of stated interest and other expense amounts owed to related foreign persons. The related-foreign-person rule is modified by Treasury regulations that provide that in the case of OID, stated interest, or other amounts owed to a related foreign person that is a FPHC, CFC or PFIC, a deduction is allowed as of the day on which the amount is	under this proposal are allowed when the amounts are paid. For purposes of determining how much of the amount accrued, if any, is currently includible in the income of a U.S. person under the relevant inclusion rules, properly allowable deductions of the related foreign corporation under the principles of section 954(b)(5) and qualified deficits under section 952(c)(1)(B) are taken into account. The Secretary is granted regulatory authority to provide exceptions to these rules, including an exception for amounts accrued where payment of the amount accrued occurs within a short period after accrual, and the transaction giving rise to the payment is entered into by the payor in the ordinary course of a business in which the payor is predominantly engaged. Effective date.–Payments accrued on or after date of enactment.	

Provision	Present Law	House Bill	Senate Amendment
	includible in the income of the FPHC, CFC or PFIC, respectively.		
18. Exclusion from gross income for interest on overpayments of income tax by individuals (sec. 643 of the House bill)	Interest is required to be included in gross income. Interest on overpayments of Federal income tax is required to be included in taxable income in the same manner as any other interest that is received by the taxpayer.	Excludes overpayment interest that is paid to individual taxpayers on overpayments of Federal income tax from gross income. The exclusion from income of overpayment interest does not apply if the Secretary determines that the taxpayer's principal purpose for overpaying his or her tax is to take advantage of the exclusion. <u>Effective date</u>.–Interest received in calendar years beginning after the date of enactment.	No provision.
19. Deposits made to suspend the running of interest on potential underpayments (sec. 644 of the House bill and sec. 486 of the Senate amendment)	The taxpayer may make a deposit in the nature of a cash bond to stop the running of interest on an amount of underpayment equal to the deposit, but the deposit does not itself earn interest.	Allows a taxpayer to deposit cash with the IRS that may subsequently be used to pay an underpayment of taxes. Interest will not be charged on the portion of the underpayment that is deposited for the period that the amount is on deposit. Generally, deposited amounts that have not been used to pay a tax may be withdrawn at any time if the taxpayer so requests in writing. The withdrawn amounts will earn interest at the applicable Federal	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
		rate to the extent they are attributable to a disputable tax. Effective date.–Deposits made after date of enactment.	
20. Authorize IRS to enter into installment agreements that provide for partial payment (sec. 645 of the House bill and sec. 484 of the Senate amendment)	The Code authorizes the IRS to enter into written agreements with any taxpayer under which the taxpayer is allowed to pay taxes owed, as well as interest and penalties, in installment payments if the IRS determines that doing so will facilitate collection of the amounts owed. Prior to 1998, the IRS administratively entered into installment agreements that provided for partial payment (rather than full payment) of the total amount owed over the period of the agreement. In that year, the IRS Chief Counsel issued a memorandum concluding that partial payment installment agreements were not permitted.	Clarifies that the IRS is authorized to enter into installment agreements with taxpayers which do not provide for full payment of the taxpayer's liability over the life of the agreement. Requires the IRS to review partial payment installment agreements at least every two years. Effective date.–Installment agreements entered into on or after the date of enactment.	Same as the House bill.
21. Affirmation of consolidated return authority (sec. 646 of the House bill and sec. 421 of the Senate amendment)	The Federal Circuit Court, in the case of *Rite Aid Corp. v. United States*, 255 F.3d 1357 (Fed. Cir. 2001), held that a provision of the Treasury Department's	Confirms that in exercising its authority under section 1502 to issue consolidated return regulations, the Treasury Department may provide rules	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
	consolidated return regulations was invalid. The court's language suggested in part that the Treasury Department may not have the authority to issue regulations that produced a result different than the result that would have obtained if the corporations had filed separate returns rather than consolidated returns.	treating corporations filing consolidated returns differently from corporations filing separate returns. Nevertheless, the result in *Rite-Aid Corp. v. United States* is allowed to stand with respect to the type of factual situation presented in the case. Effective date.–Taxable years beginning before, on, or after the date of enactment.	
22. **Reform of tax treatment of leasing transactions with tax indifferent parties (secs. 647-649 of the House bill and secs. 475 and 476 of the Senate amendment)**	Recovery period for tax-exempt use property subject to lease Tax-exempt use property subject to a lease must be depreciated on a straight-line basis over a recovery period equal to the longer of the property's class life or 125 percent of the lease term. "Tax-exempt use property" is tangible property that is leased (other than under a short-term lease) to a tax-exempt entity (including governments, charities, and foreign entities). The recovery period for qualified technological equipment ("QTE") that is treated as tax-exempt use property, and is not eligible for the QTE short-term lease exception (i.e., generally leases of five years or less), is five years.	Recovery period for tax-exempt use property subject to lease Applies the minimum recovery period for tax-exempt use property (125 percent of the lease term) to: (1) QTE leased to a tax-exempt entity (unless the lease is eligible for the present-law QTE short-term lease exception); and (2) computer software leased to a tax-exempt entity (unless the lease is eligible for the present-law QTE short-term exception). Also provides that the lease term includes all service contracts and other similar arrangements that follow a lease of property to a tax-exempt entity and that are part of	Recovery period for tax-exempt use property subject to lease Same as House bill, except: (1) does not except lessee renewal or extension options of up to 24 months from the determination of whether a QTE lease satisfies the present-law QTE short-term lease exception; and (2) the effective date. Effective date.–Leases entered into after December 31, 2003.

Provision	Present Law	House Bill	Senate Amendment
	In determining the lease term for purposes of the 125-percent calculation, taxpayers must include options to renew, and two or more successive leases with respect to the same or similar property are treated as one lease.	the same transaction (or series of transactions) as the lease. For purposes of determining whether a QTE lease satisfies the present-law QTE short-term lease exception, also provides that the lease term generally does not include certain renewal or extension options of the lessee, provided the aggregate period of such renewals or extensions does not exceed 24 months. <u>Effective date</u>.–Leases entered into after March 12, 2004, except for leases of domestic property if a formal approval application that includes a description and fair market value of the leased property is submitted to the Federal Transit Administration between July 1, 2003 and March 12, 2004, and the application is approved before January 1, 2005. The like-kind exchange and involuntary conversion rules are effective with respect to property exchanged or converted after the date of enactment.	

Provision	Present Law	House Bill	Senate Amendment
	<u>Limitation on deductions allocable to property used by governments or other tax-exempt entities</u> Depreciation and other deductions or losses allocable to tax-exempt property are not limited to the income from the property.	<u>Limitation on deductions allocable to property used by governments or other tax-exempt entities</u> Provides that if a taxpayer leases property to a tax-exempt entity, the taxpayer may not claim deductions or losses from the lease transaction in excess of the taxpayer's gross income from the lease for that taxable year. Disallowed deductions are carried forward and treated as deductions related to the lease in the following taxable year subject to the same limitations, and are allowable upon complete disposition of the leased property. Also provides that this limitation does not apply to certain transactions involving low-income housing credit property or rehabilitation credit property. A lease of property to a tax-exempt party is not subject to this limitation if the lease satisfies all of the following requirements: (1) the tax-exempt lessee does not monetize or defease its lease obligations in an amount that exceeds (a) 20 percent of the taxpayer's adjusted basis in the leased property at the time the lease is entered into, (b) 50 percent	<u>Limitation on deductions allocable to property used by governments or other tax-exempt entities</u> Similar to House bill, except: (1) does not provide an exception for rehabilitation credit property; (2) requires (a) that the leased property not be financed with tax-exempt bonds or Federal funds, (b) that any lease of property with a class life of more than seven years not include a fixed-price purchase option of the lessee, and (c) that the lease meet any other requirements prescribed in regulations; (3) permits the Secretary to identify arrangements (in addition to those specified by statute) to which the monetization and defeasance requirement applies; (4) provides only a partial exception from the equity investment requirement for short-term leases (rather than a complete exception for leases with lease terms of five years or less); (5) does not provide an exception from the minimal risk of loss requirement for leases with lease terms of five years or less; (6) does not provide special rules relating to like-kind exchanges and involuntary conversions; and (7) the effective date.

Provision	Present Law	House Bill	Senate Amendment
		of such basis if the Secretary determines that the creditworthiness of the tax-exempt entity necessitates such increase, or (c) zero percent of such basis in the case of certain lease arrangements that involve circular cash flows or insulation of the taxpayer's equity investment from the risk of loss; (2) except for leases with lease terms of five years or less, the taxpayer makes and maintains at least a 20-percent equity investment in the leased property and the fair market value of the property at the end of the lease term is reasonably expected to decline by no more than 80 percent; (3) except for leases with lease terms of five years or less, the tax-exempt lessee does not bear more than a minimal risk of loss (i.e., requirement not satisfied if the lessee bears any of the first 25 percent of loss or more than 50 percent of the overall loss associated with a potential decline in the property's market value). Also provides special rules to prevent the circumvention of this limitation through the use of like-kind exchanges and involuntary conversions.	

Provision	Present Law	House Bill	Senate Amendment
		Effective date.–Leases entered into after March 12, 2004, except for leases of domestic property if a formal approval application that includes a description and fair market value of the leased property is submitted to the Federal Transit Administration between July 1, 2003 and March 12, 2004, and the application is approved before January 1, 2005. The like-kind exchange and involuntary conversion rules are effective with respect to property exchanged or converted after the date of enactment.	Effective date.–Leases entered into after November 18, 2003, and with respect to property leased to foreign lessees, taxable years beginning after January 31, 2004, with respect to leases entered into on or before November 18, 2003.
23. Clarification of economic substance doctrine and penalty for understatements attributable to transactions lacking economic substance (secs. 401 and 404 of the Senate amendment)	Courts have developed several common law doctrines that can be applied to deny the tax benefits of tax-motivated transactions, notwithstanding that the transaction may satisfy the literal requirements of a specific statutory tax provision. A common law doctrine applied with increasing frequency is the "economic substance" doctrine. In general, this doctrine denies tax benefits arising from tax-motivated transactions that do not result in a meaningful change to the taxpayer's economic position other than a purported reduction in Federal income tax.	No provision.	Provides that, in any case in which a court determines that the economic substance doctrine is relevant to a transaction, the transaction satisfies the economic substance doctrine only if: (1) the transaction changes in a meaningful way (apart from Federal income tax consequences) the taxpayer's economic position; and; (2) the taxpayer has a substantial non-tax purpose for entering into such transaction and the transaction is a reasonable means of accomplishing such purpose.

Provision	Present Law	House Bill	Senate Amendment
	No penalties are specifically applicable to transactions that result in an understatement of tax solely by virtue of lacking economic substance.		Provides that potential profit may not be relied on to establish economic substance unless: (1) reasonably expected pre-tax profit is substantial in relation to present value of expected net tax benefits and; (2) it exceeds a risk-free rate of return. Fees and foreign taxes taken into account as expenses. Financing transactions with tax-indifferent parties not respected if present value of deductions to be claimed is substantially in excess of present value of anticipated economic returns of tax-indifferent party. Artificial income shifting to tax-indifferent party not respected. Imposes a separate 40-percent penalty on understatements of tax resulting from transactions that lack economic substance, and limits the ability to assert or compromise and an asserted penalty. The penalty is reduced to 20 percent for disclosed transactions. Requires a publicly traded entity that is required to pay a penalty for an understatement of tax with respect to a transaction that lacks economic substance to disclose the imposition of the penalty in reports to the SEC. Also requires the

Provision	Present Law	House Bill	Senate Amendment
			Secretary to make public the name of any person required to pay such penalty and the amount of such penalty. Effective date.–Transactions entered into after the date of enactment.
24. Understatement of taxpayer's liability by income tax return preparer (sec. 411 of the Senate amendment)	An income tax return preparer who prepares a return with respect to which there is an understatement of tax that is due to an undisclosed position for which there was not a realistic possibility of being sustained on its merits, or a frivolous position, is liable for a penalty of $250, provided the preparer knew or reasonably should have known of the position. An income tax return preparer who prepares a return and engages in specified willful or reckless conduct with respect to preparing such a return is liable for a penalty of $1,000.	No provision.	Alters the standards of conduct that must be met to avoid imposition of the first penalty by replacing the realistic possibility standard with a requirement that there be a reasonable belief that the tax treatment of the position was more likely than not the proper treatment. Also replaces the not frivolous standard with the requirement that there be a reasonable basis for the tax treatment of the position. Also increases the amount of these penalties. Effective date.–Documents prepared after the date of enactment.
25. Frivolous tax submissions (sec. 413 of the Senate amendment)	An individual who files a frivolous income tax return is subject to a penalty of $500. The Tax Court also may impose a penalty of up to $25,000 if a taxpayer has instituted	No provision.	Modifies the penalty by increasing the amount of the $500 penalty to a maximum of $5,000 and applying it to all taxpayers and to all types of Federal taxes. Also modifies

Provision	Present Law	House Bill	Senate Amendment
	or maintained proceedings primarily for delay or if the taxpayer's position in the proceeding is frivolous or groundless.		present law with respect to certain submissions that raise frivolous arguments or that are intended to delay or impede tax administration. Effective date.–Submissions made and issues raised after the date on which the Secretary first prescribes the required list of frivolous positions.
26. Authorization of appropriations for tax law enforcement (sec. 418 of the Senate amendment)	There is no explicit authorization of appropriations to the IRS to be used to combat abusive tax avoidance transactions.	No provision.	Authorizes an additional $300 million to the IRS to be used to combat abusive tax avoidance transactions. Effective date.–Date of enactment.
27. Study on information sharing among law enforcement agencies (sec. 420 of the Senate amendment)	No provision.	No provision.	Requires the Treasury Secretary, jointly with the Attorney General, the SEC, and the IRS Commissioner, to study the effectiveness of, and ways to improve, the sharing of information related to the promotion of prohibited tax shelters or tax avoidance schemes and other potential violations of Federal laws. Also requires the Treasury Secretary to report to the appropriate committees of

Provision	Present Law	House Bill	Senate Amendment
			Congress the results of the study, including any legislative recommendations, within one year after the date of enactment.
28. Declaration by chief executive officer relating to Federal annual corporate income tax return (sec. 422 of the Senate amendment)	The income tax return of a corporation must be signed by either the president, the vice-president, the treasurer, the assistant treasurer, the chief accounting officer, or any other officer of the corporation authorized by the corporation to sign the return. A criminal penalty is imposed on any person who willfully signs any tax return under penalties of perjury that that person does not believe to be true and correct with respect to every material matter at the time of filing.	No provision.	Requires the Federal income tax return of a corporation (other than that of a regulated investment company) also to include a declaration signed, under penalties of perjury, by the chief executive officer of the corporation that the corporation has in place processes and procedures that ensure the return is compliant and that the chief executive officer was provided reasonable assurance of the accuracy of all material aspects of the return. <u>Effective date</u>.–Federal tax returns for taxable years ending after the date of enactment.
29. Denial of deduction for certain fines, penalties, and other amounts (sec. 423 of the Senate amendment)	No deduction is allowed as a trade or business expense under section 162(a) for the payment of a fine or similar penalty to a government for the violation of any law. Treasury regulations provide that nondeductibility applies to settlement payments. However,	No provision.	Provides that amounts paid or incurred, to or at the direction of a government in relation to the violation of any law or the governmental investigation or inquiry into the potential violation of any law, are nondeductible under any income tax provision.

Provision	Present Law	House Bill	Senate Amendment
	there is a lack of clarity and consistency regarding when taxpayers may deduct payments in settlements, including cases where there has been no final determination of wrongdoing.		Thus, a taxpayer may not avoid nondeductibility of a settlement payment by not admitting wrongdoing, or by characterizing the payment as a charitable deduction rather than as a business expense. An exception applies to payments that are for restitution or for remediation of property Effective date.–Amounts paid or incurred on or after April 28, 2003, unless paid under a binding order or agreement entered before that date. If court approval is required, an order or agreement is not considered binding until such court approval is obtained.
30. Disallowance of deduction for punitive damages (sec. 424 of the Senate amendment)	A deduction generally is allowed for all ordinary and necessary expenses that are paid or incurred by the taxpayer during the taxable year in carrying on any trade or business, including the payment of punitive damages. In general, gross income does not include amounts received on account of personal physical injuries and physical sickness. However, this exclusion does not apply to punitive damages.	No provision.	Denies any deduction for punitive damages that are paid or incurred by the taxpayer as a result of a judgment or in settlement of a claim. If the liability for punitive damages is covered by insurance, any such punitive damages paid by the insurer are included in gross income of the insured person and the insurer is required to report such amounts to both the insured person and the IRS.

Provision	Present Law	House Bill	Senate Amendment
			Effective date.–Punitive damages paid or incurred on or after the date of enactment.
31. Expanded disallowance of deduction for interest on convertible debt (sec. 434 of the Senate amendment)	No deduction is allowed for interest or Original Issue Discount ("OID") on a debt instrument issued by a corporation (or issued by a partnership to the extent of its corporate partners) that is payable in equity of the issuer or a related party (defined to include a person related to the issuer through equity that represents more than a 50-percent ownership interest), including a debt instrument a substantial portion of which is mandatorily convertible or convertible at the issuer's option into equity of the issuer or a related party. In addition, a debt instrument is treated as payable in equity if a substantial portion of the principal or interest is required to be determined, or may be determined at the option of the issuer or related party, by reference to the value of equity of the issuer or related party.	No provision.	Generally expands the present-law disallowance of interest deductions to include interest on corporate debt that is payable in, or by reference to the value of, any equity held by the issuer (or any related party) in any other person, without regard to whether such equity represents more than a 50-percent ownership interest in such person. The basis of such equity is increased by the amount of interest deductions that is disallowed by the provision. Effective date.–Debt instruments issued after February 13, 2003.

Provision	Present Law	House Bill	Senate Amendment
32. Increase in criminal monetary penalty limitation for the underpayment or overpayment of tax due to fraud (sec. 425 of the Senate amendment)	<u>Attempt to evade or defeat tax</u> A criminal penalty generally is imposed on persons who willfully attempt to evade or defeat any tax imposed by the Code. Upon conviction, the Code provides that the penalty is up to $100,000 or imprisonment of not more than five years (or both). In the case of a corporation, the Code increases the monetary penalty to a maximum of $500,000. <u>Willful failure to file return, supply information, or pay tax</u> A criminal penalty generally is imposed on persons required to make estimated tax payments, pay taxes, keep records, or supply information under the Code who willfully fails to do so. Upon conviction, the Code provides that the penalty is up to $25,000 or imprisonment of not more than one year (or both). In the case of a corporation, the Code increases the monetary penalty to a maximum of $100,000.	No provision.	<u>Attempt to evade or defeat tax</u> Increases the criminal penalty under section 7201 of the Code for individuals to $250,000 and for corporations to $1,000,000. The provision increases the maximum prison sentence to ten years. <u>Willful failure to file return, supply information, or pay tax</u> Increases the criminal penalty under section 7203 of the Code from a misdemeanor to a felony and increases the maximum prison sentence to ten years.

Provision	Present Law	House Bill	Senate Amendment
	<u>Fraud and false statements</u> A criminal penalty generally is imposed on persons who make fraudulent or false statements under the Code. Upon conviction, the Code provides that the penalty is up to $100,000 or imprisonment of not more than three years (or both). In the case of a corporation, the Code increases the monetary penalty to a maximum of $500,000. <u>Uniform sentencing guidelines</u> The uniform sentencing guidelines can provide for substantial increases in the levels of monetary penalties and are applicable to all criminal provisions in the United States Code, including those in the Code.		<u>Fraud and false statements</u> Increases the criminal penalty under section 7206 of the Code for individuals to $250,000 and for corporations to $1,000,000. Increases the maximum prison sentence to five years. Provides that in no event shall the amount of the monetary penalty under this provision be less than the amount of the underpayment or overpayment attributable to fraud. <u>Effective date</u>.–Underpayments and overpayments attributable to actions occurring after the date of enactment.
33. Expanded authority to disallow tax benefits under section 269 (sec. 435 of the Senate amendment)	If a taxpayer acquires, directly or indirectly, control (defined as at least 50 percent of vote or value) of a corporation, and the principal purpose of the acquisition is the evasion or avoidance of Federal income tax by securing the benefit of a deduction, credit, or other allowance that would not otherwise have been available, such tax	No provision.	Repeals the requirement that the acquisition of property be from a corporation not controlled by the acquirer. Thus, disallows the tax benefits of: (1) any acquisition of stock sufficient to obtain control of a corporation (as under present law); and (2) any acquisition by a corporation of property from a corporation in which the basis of

Provision	Present Law	House Bill	Senate Amendment
	benefits may be disallowed. Similarly, if a corporation acquires, directly or indirectly, property of another corporation (not controlled, directly or indirectly, by the acquiring corporation or its stockholders immediately before the acquisition), the basis of such property is determined by reference to the basis in the hands of the transferor corporation, and the principal purpose of the acquisition is the evasion or avoidance of Federal income tax by securing a tax benefit that would not otherwise have been available, such tax benefits may be disallowed.		such property is determined by reference to the basis in the hands of the transferor corporation, if the principal purpose of such acquisition is the evasion or avoidance of Federal income tax. Effective date.–Stock and property acquired after February 13, 2003.
34. Modification of interaction between subpart F and passive foreign investment company rules (sec. 5646 of the Senate amendment)	Under an anti-overlap rule, a controlled foreign corporation generally is not also treated as a passive foreign investment company with respect to a U.S. shareholder of the corporation, regardless of the likelihood that the U.S. shareholder would actually be taxed under subpart F in the event that the controlled foreign corporation earns subpart F income.	No provision.	Adds an exception to the anti-overlap rule for U.S. shareholders that face only a remote likelihood of incurring a subpart F inclusion in the event that a controlled foreign corporation earns subpart F income, thus preserving the potential application of the passive foreign investment company rules in such cases. Effective date.–Taxable years of controlled foreign corporations beginning after February 13, 2003, and taxable years of U.S.

Provision	Present Law	House Bill	Senate Amendment
			shareholders in which or with which such taxable years of controlled foreign corporations end.
C. Deferred Compensation Provisions **1. Treatment of nonqualified deferred compensation plans (sec. 671 of the House bill and sec. 671 of the Senate amendment)**	The determination of when amounts deferred under a nonqualified deferred compensation arrangement are includible in the gross income of the individual earning the compensation depends on the facts and circumstances of the arrangement. A variety of tax principles and Code provisions may be relevant in making this determination, including the doctrine of constructive receipt, the economic benefit doctrine, the provisions of section 83 relating generally to transfers of property in connection with the performance of services, and provisions relating specifically to nonexempt employee trusts and nonqualified annuities. While the general tax principles governing deferred compensation are well established, the determination whether a particular arrangement effectively allows deferral of income is generally made on a facts and circumstances basis.	All amounts deferred under a nonqualified deferred compensation plan for all taxable years are currently includible in gross income to the extent not subject to a substantial risk of forfeiture, unless certain requirements relating to permissible distributions and elections are satisfied. Distributions may be allowed only upon separation from service, death, disability, specified time, change in control or unforeseeable emergency. Assets set aside in an offshore trust are treated as property transferred under section 83. A transfer of property also occurs if a plan provides that assets will be restricted upon a change in financial health. If the requirements of the provision are not satisfied, in addition to current income inclusion, interest at the underpayment rate plus one	Similar to House bill, with certain modifications. Payments made to individuals subject to section 16(a) of the Securities and Exchange Act of 1934 within one year of a change in control are treated as excess parachute payments. Unforeseeable emergency also includes hardship to the beneficiary. Participants must be limited to one subsequent election. Limits on investment direction apply. Provision does not apply to plans meeting the exception under section 457(e)(12) as of May 1, 2004. If the requirements of the provision are not satisfied, in addition to current income inclusion, interest at the underpayment rate is

Provision	Present Law	House Bill	Senate Amendment
		percentage point is imposed on the underpayments that would have occurred had the compensation been includible in income when first deferred, or if later, when not subject to a substantial risk of forfeiture. Effective date.–Amounts deferred after June 3, 2004, except for amounts deferred before January 1, 2005, pursuant to an irrevocable election or binding arrangement made before June 4, 2004.	imposed on the underpayments that would have occurred had the compensation been includible in income when first deferred, or if later, when not subject to a substantial risk of forfeiture. A ten percent additional tax also applies. Effective date.–Amounts deferred in taxable years beginning after December 31, 2004.
2. Prohibition on deferral of gain from the exercise of stock options and restricted stock (sec. 672 of the Senate amendment)	Under section 83, if, in connection with the performance of services, property is transferred to any person other than the person for whom such services are performed, the excess of the fair market value of such property over the amount (if any) paid for the property is includible in income at the first time that the property is transferable or not subject to substantial risk of forfeiture. Nonqualified stock options and stock granted to an employee are subject to the rules that apply under section 83.	No provision.	If a taxpayer exchanges: (1) employer securities; (2) an option to purchase employer securities; or (3) any other property based on employer securities, for a right to receive future payments, an amount equal to the present value of such right (or such other amount as the Secretary specifies) is required to be included in gross income for the taxable year of the exchange. Effective date.–Exchanges made after December 31, 2004.

Provision	Present Law	House Bill	Senate Amendment
D. Other Revenue Provisions **1. Permit private sector debt collection companies to collect tax debts (sec. 681 of the House bill and sec. 487 of the Senate amendment)**	In general, Federal agencies are permitted to enter into contracts with private debt collection companies for collection services to recover indebtedness owed to the United States. That provision does not apply to the collection of debts under the Internal Revenue Code.	Permits the IRS to use private debt collection companies to locate and contact taxpayers owing outstanding tax liabilities and to arrange payment of those taxes by the taxpayers. If the taxpayer cannot pay in full immediately, the private debt collection company offers the taxpayer an installment agreement providing for full payment of the taxes over five years. If the taxpayer is unable to pay the outstanding tax liability in full over a five-year period, the private debt collection company obtains financial information from the taxpayer and will provide this information to the IRS for further processing and action by the IRS. Creates a revolving fund from the amounts collected by the private debt collection companies. The private debt collection companies would be paid out of this fund. <u>Effective date.</u>–Date of enactment.	Same as the House bill, except: (1) sunsets provision in five years; (2) provides that, if the taxpayer cannot pay in full immediately, the private debt collection company may offer the taxpayer an installment agreement providing for full payment of the taxes over three years; (3) provides that up to 25 percent of amount collected may be used for IRS collection enforcement activities; (4) and requires a biennial report.

Provision	Present Law	House Bill	Senate Amendment
2. Modify charitable contribution rules for donations of patents and similar intellectual property (sec. 682 of the House bill and sec. 494 of the Senate amendment)	For charitable contributions of capital gain property, the amount of the deduction generally equals the fair market value of the contributed property on the date of the contribution. For contributions of ordinary income property, the taxpayer is required to reduce the deduction amount by any gain, generally resulting in a deduction equal to the taxpayer's basis. Capital gain property generally means any property the sale of which at the time of contribution would have resulted in long-term capital gain. In general, patents and similar intellectual property are considered capital gain property, in which case a fair market value deduction generally is available for charitable contributions of such assets. Certain copyrights are not considered capital gain property, in which case the charitable deduction for such copyrights generally is limited to the taxpayer's basis. Taxpayers that understate tax liability on a return due to a valuation misstatement are subject to a penalty of 20 percent of the underpayment in the case of a substantial valuation misstatement,	The provision provides that if a taxpayer contributes a patent or other intellectual property (other than certain copyrights or inventory) to a charitable organization, the taxpayer's initial charitable deduction is limited to the lesser of the taxpayer's basis in the contributed property or the fair market value of the property. In addition, the taxpayer is permitted to deduct, as a charitable deduction, certain additional amounts in the year of contribution or in subsequent taxable years based on a specified percentage of the net income received or accrued by the charitable donee that properly is allocable to the contributed property itself (as opposed to the activity in which the contributed property is used). An additional charitable deduction is allowed only to the extent that the aggregate of the amounts that are calculated pursuant to the specified percentage exceed the amount of the deduction claimed upon the contribution of the patent or intellectual property. No charitable deduction is permitted with respect to any	Similar to House bill, except that the taxpayer's initial deduction is equal to: the lesser of the taxpayer's basis in the contributed property or the fair market value of the property (as in the House bill) <u>or</u>, if greater, the lesser of 5 percent of the fair market value of the contributed property or $1 million. Additional charitable deductions are available as in the House bill, except that such additional deductions are not required to be offset by the initial deductible amount. The Senate amendment imposes a processing fee (credited to the Exempt Organizations unit with the IRS) equal to 1 percent of the claimed deductible amount for contributions of applicable intellectual property. With respect to applicable intellectual property contributions, the Senate amendment increases the present law thresholds that trigger application of penalties for substantial and gross valuation misstatements. The substantial misstatement penalty applies if the taxpayer's claimed value exceeds

Provision	Present Law	House Bill	Senate Amendment
	and 40 percent of the underpayment in the case of a gross valuation misstatement. A substantial misstatement occurs if the taxpayer's claimed value is 200 percent or more of the correct amount. A gross misstatement occurs if the taxpayer's claimed value is 400 percent or more of the correct amount.	revenues or income received or accrued by the charitable donee after the expiration of the legal life of the patent or intellectual property, or after the tenth anniversary of the date the contribution was made by the donor. Effective date.–Contributions after June 3, 2004.	the correct amount by 50 percent or more; the gross misstatement penalty applies if the taxpayer's claimed value exceeds the correct amount by 100 percent or more. The Senate amendment requires that the Secretary shall prescribe guidance on appraisal standards for charitable contributions of intellectual property. Effective date.–Contributions after the date of enactment.
3. Require increased reporting for noncash charitable contributions (sec. 683 of the House bill)	In general, if a taxpayer deducts more than $500 for a charitable contribution of non-cash property, the taxpayer must file Form 8283 with the IRS. A qualified appraisal is required for donated property (other than money and publicly traded securities) worth more than $5,000. C corporations (other than personal service corporations and closely-held corporations) must file Form 8283 only if the deduction exceeds $5,000 and are not required to obtain a qualified appraisal. The qualified appraisal must accompany the taxpayer's	Extends to all C corporations the present-law requirement that the donor must obtain a qualified appraisal of the property if the deduction exceeds $5,000. If the value of contributed property other than cash, inventory, or publicly traded securities exceeds $500,000, the qualified appraisal must accompany the donor's return. No deduction is allowed to a donor that fails to substantiate a contribution of property. Effective date.–Contributions after June 3, 2004.	No provision.

Provision	Present Law	House Bill	Senate Amendment
	return only for contributions of art work valued at more than $20,000.		
4. Modify charitable contribution rules for donations of vehicles (sec. 684 of the House bill and sec. 731 of the Senate amendment)	For charitable contributions of personal property, such as an automobile, in which basis exceeds value, the amount of the deduction equals the value of the property on the date of the contribution. Taxpayers are required to obtain a qualified appraisal for donated property with a value of $5,000 or more.	A deduction is allowed for charitable contributions of vehicles (generally including automobiles, boats, and aircraft and not inventory property) for which the taxpayer claims a deduction of more than $250 only if the taxpayer obtains a qualified appraisal of the vehicle by the time the contribution is made. Effective date.–Contributions after June 3, 2004.	A deduction for charitable contributions of vehicles (generally including automobiles, boats, and airplanes and not inventory property) generally may not exceed the price for which the vehicle is sold by the donee. The donee must notify the donor and the IRS of the gross proceeds from the sale, and that the donor's deduction may not exceed such gross proceeds. If the donee does not sell the vehicle, or sells the vehicle after a significant use or material improvement by the donee, the deduction may not exceed the value of the property at the time of the contribution. The donee must notify the taxpayer and the IRS of the donee's intended use. Monetary penalties apply to fraudulent notices knowingly furnished by the donee. Effective date.–Contributions after June 30, 2004.

Provision	Present Law	House Bill	Senate Amendment
5. Extension of amortization of intangibles to sports franchises (sec. 685 of the House bill and sec. 471 of the Senate amendment)	Intangible assets acquired in connection with the acquisition of a trade or business generally are recovered over 15 years. An exception exists for intangibles acquired in connection with a pro sports franchise. With respect to a sports franchise acquisition, basis allocated to assets with determinable useful lives (such as player contracts) is recovered over the assets' respective useful lives. Basis allocated to the franchise or to other intangible assets acquired with the franchise may not be amortizable if these assets lack a determinable useful life. Present law also provides related special rules for sports franchises, including: (1) a limitation on the amount of basis which taxpayers may allocate to player contracts; (2) special rules for recapture on disposition of player contracts; and (3) an exception from section 1253, which treats gain on the sale of a franchise as ordinary income if the transferor retains significant power, right, or continuing interest with respect to the subject matter of the franchise.	Extends the 15-year recovery period for intangible assets to sports franchises and any intangible asset acquired in connection with the acquisition of such a franchise (including player contracts). Repeals other special rules for sports franchises relating to: (1) the basis limitation for player contracts; (2) the recapture of ordinary income on disposition of player contracts; and (3) the exception for sports franchises from the general rule of section 1253. Thus, the same rules for amortization of intangibles that apply to other acquisitions under present law will apply to acquisitions of sports franchises. Effective date.–Property acquired after the date of enactment.	Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
6. Increase continuous levy for certain federal payments (sec. 686 of the House bill and 734 of the Senate amendment)	If any person is liable for any tax and does not pay it, the IRS may generally collect the tax by levy. A continuous levy of up to 15 percent is applicable to specified Federal payments.	Permits a levy of up to 100 percent of a Federal payment to a vendor of goods or services to the Federal Government. <u>Effective date.</u>–Date of enactment.	Same as the House bill.
7. Modification of straddle rules (sec. 687 of the Hosue bill and sec. 464 of the Senate amendment)	When a taxpayer realizes a loss with respect to a position in a straddle (i.e., offsetting positions with respect to actively traded personal property), the taxpayer may recognize that loss for any taxable year only to the extent that the loss exceeds any unrecognized gain with respect to offsetting positions in the straddle. Deferred losses are carried forward to the succeeding taxable year and are subject to the same limitation with respect to unrecognized gain in offsetting positions. In limited cases, the straddle rules do not apply to positions in stock. Also, the straddle rules do not apply to offsetting positions that consist of stock and an option if the option is a "qualified covered call option" written by the taxpayer.	Modifies the straddle rules as follows: (1) permits taxpayers to identify offsetting positions of a straddle (including an unbalanced straddle) and provides for capitalization (rather than deferral) of losses attributable to such straddles; (2) clarifies the present-law treatment of certain physically settled positions of a straddle; (3) repeals the stock exception; and (4) excludes in-the-money qualified covered call options from exceptions to holding period tolling rules elsewhere in the Code. <u>Effective date</u>.–Positions established on or after the date of enactment.	Same as the House bill, except also limits the present-law qualified covered call exception to options traded on national securities exchanges registered with the SEC.

Provision	Present Law	House Bill	Senate Amendment
	The Treasury Secretary is directed to provide regulations concerning straddles in which one position offsets only a portion of one or more other positions ("unbalanced straddles"). To date, no such regulations have been promulgated.		
8. Add vaccines against Hepatitis A to the list of taxable vaccines (sec. 688 of the House bill and sec. 491 of the Senate amendment)	A manufacturer's excise tax is imposed at the rate of 75 cents per dose on the following vaccines routinely recommended for administration to children: diphtheria, pertussis, tetanus, measles, mumps, rubella, polio, HIB (haemophilus influenza type B), hepatitis B, varicella (chicken pox), rotavirus gastroenteritis, and streptococcus pneumoniae. Amounts equal to net revenues from this excise tax are deposited in the Vaccine Injury Compensation Trust Fund to finance compensation awards under the Federal Vaccine Injury Compensation Program for individuals who suffer certain injuries following administration of the taxable vaccines.	Adds any vaccine against hepatitis A to the list of taxable vaccines. Effective date.–Effective for vaccines sold beginning on the first day of the first month beginning more than four weeks after the date of enactment.	Similar to House bill. In addition to adding vaccines against hepatitis A to the list of taxable vaccines, the Senate amendment also modifies Vaccine Injury Compensation Trust Fund expenditure purposes. Effective date.–Same as the House bill.

Provision	Present Law	House Bill	Senate Amendment
9. Add vaccines against influenza to the list of taxable vaccines (sec. 689 of the House bill and sec. 732 of the Senate amendment)	A manufacturer's excise tax is imposed at the rate of 75 cents per dose on the following vaccines routinely recommended for administration to children: diphtheria, pertussis, tetanus, measles, mumps, rubella, polio, HIB (haemophilus influenza type B), hepatitis B, varicella (chicken pox), rotavirus gastroenteritis, and streptococcus pneumoniae. Amounts equal to net revenues from this excise tax are deposited in the Vaccine Injury Compensation Trust Fund to finance compensation awards under the Federal Vaccine Injury Compensation Program for individuals who suffer certain injuries following administration of the taxable vaccines.	Adds any trivalent vaccine against influenza to the list of taxable vaccines. <u>Effective date</u>.–Effective for vaccines sold or used beginning on the later of the first day of the first month beginning more than four weeks after the date of enactment or the date on which the Secretary of Health and Human Services lists any such vaccine for purpose of compensation for any vaccine-related injury or death through the Vaccine Injury Compensation Trust Fund.	Same as the House bill.
10. Extension of IRS user fees (sec. 690 of the House bill and sec. 482 of the Senate amendment)	The IRS generally charges a fee for requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination. These user fees are authorized by statute through December 31, 2004.	Extends the statutory authorization for these user fees through September 30, 2014. <u>Effective date</u>.–Requests made after the date of enactment.	Same as the House bill, except extends the statutory authorization for these user fees through September 30, 2013.

Provision	Present Law	House Bill	Senate Amendment
11. Extension of customs user fees (sec. 691 of the House bill and sec. 485 of the Senate amendment)	Section 13031 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), authorized the Secretary of the Treasury to collect certain service fees. Section 412 of the Homeland Security Act of 2002 authorized the Secretary of the Treasury to delegate such authority to the Secretary of Homeland Security. Pub. L. No. 108-121 extended authorization for the collection of these fees through March 1, 2005.	<u>Extension of fees</u>.–Extends the passenger and conveyance processing fees and the merchandise processing fees authorized under the Consolidated Omnibus Budget Reconciliation Act of 1985 through September 30, 2014. For fiscal years after September 30, 2005, the Secretary is to charge fees in amount that are reasonably related to the costs of providing services. <u>Sense of Congress</u>.–Includes a Sense of the Congress that the fees have been reasonably related to the costs of providing customs services. <u>Study</u>.–Provides that the Secretary conduct a study of all the fees collected by the Department of Homeland Security, and shall submit to the Congress, not later than September 30, 2005, a report containing the recommendations of the Secretary on what fees should be eliminated and what the rate of fees retained should be. <u>Effective date</u>.–Date of enactment.	<u>Extension of fees</u>.–Extends fees through September 30, 2013. <u>Sense of Congress</u>.–No provision. <u>Study</u>.–No provision. <u>Effective date</u>.–Date of enactment.

Provision	Present Law	House Bill	Senate Amendment
12. Prohibition on nonrecognition of gain through complete liquidation of holding company (sec. 452 of the Senate amendment)	A U.S. corporation owned by foreign persons is subject to U.S. income tax on its net income. In addition, when dividends are paid to the corporation's shareholders, the earnings of the U.S. corporation are subject to a withholding tax at a rate of 30 percent (that may be reduced under an income tax treaty). In general, U.S. withholding tax is not imposed with respect to a distribution of a U.S. corporation's earnings to a foreign corporation in complete liquidation of the subsidiary, because the distribution is treated as made in exchange for stock and not as a dividend. Regulations under section 367(e) provide that the Commissioner may require a domestic liquidating corporation to recognize gain on distributions in liquidation made to a foreign corporation if a principal purpose of the liquidation is the avoidance of U.S. tax.	No provision.	Treats as a dividend any distribution of earnings by a U.S. holding company to a foreign corporation in a complete liquidation, if the U.S. holding company was in existence for less than five years. <u>Effective date</u>.–Distributions occurring on or after date of enactment.

Provision	Present Law	House Bill	Senate Amendment
13. Effectively connected income to include certain foreign source income (sec. 454 of the Senate amendment)	Foreign persons are subject to U.S. tax on net income that is effectively connected with the conduct of a U.S. trade or business Effectively Connected Income ("ECI"). Foreign-source income is not generally treated as ECI unless the foreign person has an office or other fixed place of business within the United States to which such income is attributable, and if such income falls into one of three categories: (1) rents or royalties for certain intangible properties that are derived in the active conduct of the U.S. trade or business; (2) interest or dividends derived in the active conduct of a banking, financing, or similar business within the United States, or received by a corporation whose principal business is trading in stocks or securities for its own account; and (3) income derived from the sale or exchange of inventory outside the United States through the foreign	No provision.	Each category of foreign-source income that is treated as ECI is expanded to include economic equivalents of such income (i.e., economic equivalents of certain foreign-source: (1) rents and royalties; (2) interest and dividends; and (3) income on sales or exchanges of inventory). Such economic equivalents are treated as ECI in the same circumstances that foreign-source rents, royalties, dividends, interest, or certain inventory sales are treated as ECI. Effective date.–Taxable years beginning after the date of enactment.

Provision	Present Law	House Bill	Senate Amendment
	person's U.S. office or other fixed place of business.		
14. Recapture of overall foreign losses on sale of controlled foreign corporation stock (sec. 455 of the Senate amendment)	Recapture rules apply in the case of overall foreign losses ("OFL") for purposes of applying the foreign tax credit limitation. Under a special OFL recapture rule, a disposition of property which was used in a trade or business predominantly outside the United States results in the recognition of foreign-source income (regardless of whether gain would otherwise be recognized upon disposition of the assets), in an amount equal to the lesser of the excess of the fair market value of such property over its adjusted basis, or the amount of unrecaptured OFL. Such foreign-source income is resourced as U.S.-source income.	No provision.	The present-law OFL recapture rule that currently applies to dispositions of foreign trade or business assets is extended to the disposition of stock in a controlled foreign corporation controlled by the taxpayer, with exceptions for internal restructurings. Effective date.–Dispositions after the date of enactment.
15. Application of earnings stripping rules to partnerships and S corporations (sec. 462 of the Senate amendment)	Special rules limit the ability of U.S. taxable subchapter C corporations to engage in earnings stripping transactions involving interest payments. The deductibility of interest paid to certain related parties is limited if the payor's debt-equity ratio exceeds 1.5 to 1 and the payor's	No provision.	Attributes partnership debt to a corporate partner for purposes of applying the earnings stripping rules to the corporation. Effective date.–Taxable years beginning on or after the date of enactment.

Provision	Present Law	House Bill	Senate Amendment
	net interest expense exceeds 50 percent of its adjusted taxable income. The present-law earnings stripping rules do not apply to partnerships or S corporations.		
16. Recognition of cancellation of indebtedness income realized on satisfaction of debt with partnership interest (sec. 463 of the Senate amendment)	A corporation that transfers shares of its stock in satisfaction of its debt must recognize cancellation of indebtedness income in the amount that would be realized if the debt were satisfied with money equal to the fair market value of the stock. In the case of a partnership that transfers to a creditor an interest in the partnership in satisfaction of its debt, it is unclear whether the partnership is required to recognize cancellation of indebtedness income. It also is unclear whether any requirement to recognize cancellation of indebtedness income is affected if the cancelled debt is nonrecourse indebtedness.	No provision.	Provides that when a partnership transfers an interest in the partnership to a creditor in satisfaction of partnership debt, the partnership generally recognizes cancellation of indebtedness income in the amount that would be recognized if the debt were satisfied with money equal to the fair market value of the partnership interest. The provision applies without regard to whether the cancelled debt is recourse or nonrecourse indebtedness. <u>Effective date</u>.–Cancellations of indebtedness occurring on or after the date of enactment.
17. Denial of installment sale treatment for all readily tradeable debt (sec. 465 of the Senate amendment)	The installment method of accounting for gain recognition on certain deferred payment sales of property is not available if the taxpayer sells property in exchange for readily tradeable corporate or governmental debt. No similar provision prohibits the use of the	No provision.	Denies installment sale treatment with respect to all sales in which the taxpayer receives indebtedness that is readily tradeable, regardless of the nature of the issuer. Thus, for example, if the taxpayer receives readily tradeable debt of a partnership in a sale, the

Provision	Present Law	House Bill	Senate Amendment
	installment sale method where the taxpayer sells property in exchange for readily tradable debt issued by a partnership or an individual.		partnership debt is treated as payment on the installment note, and the installment sale method is unavailable to the taxpayer. Effective date.–Sales occurring on or after date of enactment.
18. Modification of treatment of transfers to creditors in divisive reorganizations (sec. 466 of the Senate amendment)	In a tax free spin off under section 355 of the Code in which the distributing corporation contributes property to the distributed corporation, no gain or loss is recognized if the property is contributed solely in exchange for stock or securities of the transferee corporation which are distributed to the transferor's shareholders. The transferor corporation also will not recognize gain if it receives money or other property that is distributed to its shareholders or creditors. The amount that may be distributed to creditors is unlimited. In addition, for divisive transactions under section 355, and for certain acquisitive reorganizations, the transferor corporation recognizes gain to the extent the liabilities assumed by the transferee exceed the basis of assets transferred.	No provision.	Limits the amount of money plus the fair market value of property that a distributing corporation can distribute to creditors without gain recognition to the amount of the basis of assets contributed to the distributed corporation. Acquisitive reorganizations are exempted from the rule that gain is recognized if the amount of liabilities assumed exceeds the basis of assets transferred. Effective date.–Transactions on or after the date of enactment.

Provision	Present Law	House Bill	Senate Amendment
19. Clarification of definition of nonqualified preferred stock (sec. 5681 of the Senate amendment)	Stock that is "nonqualified preferred stock" is treated as taxable boot in transactions that otherwise allow nontaxable receipt of stock. For this purpose, preferred stock is stock that is "limited and preferred as to dividends and does not participate in corporate growth to any significant extent."	No provision.	Clarifies that stock for which there is not a real and meaningful likelihood of actually participating in the earnings and profits of the corporation is treated as preferred for purposes of the provision. <u>Effective date</u>.–Transactions after May 14, 2003.
20. Modification of definition of controlled group of corporations (sec. 468 of the Senate amendment)	The members of a controlled group of corporations are limited to the benefits of one corporation for purposes of the graduated corporate rate brackets, the alternative minimum tax exemption, and the accumulated earnings credit. For this purpose, a brother-sister controlled group is defined as two or more corporations if five or fewer persons who are individuals, estates or trusts own (after application of attribution rules): (1) at least 80 percent of the combined voting power and value of all classes of stock; and (2) more than 50 percent of the total voting power or value of all stock, taking into account the stock ownership of	No provision.	Eliminates the 80-percent test from the brother-sister controlled group definition for purposes of determining the specified benefits. 80-percent test continues to apply to other Code provisions using the controlled group definition by reference. <u>Effective date</u>.–Taxable years beginning after date of enactment.

Provision	Present Law	House Bill	Senate Amendment
	each person only to the extent the stock ownership is identical with respect to each corporation.		
21. Class lives for utility grading costs (sec. 472 of the Senate amendment)	Under the modified accelerated cost recovery system, an asset for which no class life is provided is allowed a 7-year recovery period. Assets used in the transmission and distribution of electricity for sale are provided a class life of 30 years and a recovery period of 20 years. The cost of initially clearing and grading land improvements are specifically excluded and no separate asset class is provided for such costs. A similar situation exists with regard to clearing and grading costs associated with gas utility trunk pipelines and related storage facilities.	No provision.	Assigns a class life to depreciable electric and gas utility clearing and grading costs incurred to locate transmission and distribution lines and pipelines. The provision includes these assets in the asset classes of the property to which the clearing and grading costs relate (giving these assets a recovery period of 20 years and 15 years, respectively). <u>Effective date</u>.–Property placed in service after the date of enactment.
22. Expansion of limitation on depreciation of certain passenger automobiles (sec. 473 of the Senate amendment)	Passenger automobiles generally are recovered over five years. However, section 280F limits the annual depreciation deduction with respect to certain passenger automobiles. For purposes of the depreciation limitation, passenger automobiles are defined broadly to include any 4-wheeled vehicles	No provision.	Limits the ability of taxpayers to claim deductions under section 179 for certain vehicles not subject to section 280F to $25,000. The provision applies to sport utility vehicles rated at 14,000 pounds gross vehicle weight or less (in place of the present law 6,000 pound rating). For this purpose, a

Provision	Present Law	House Bill	Senate Amendment
	that are manufactured primarily for use on public streets, roads, and highways and which are rated at 6,000 pounds unloaded gross vehicle weight or less. In the case of a truck or a van, the depreciation limitation applies to vehicles that are rated at 6,000 pounds gross vehicle weight or less. Sports utility vehicles are treated as a truck for the purpose of applying the section 280F limitation. In lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to expense such investment, up to a limit of $100,000 per year. Passenger automobiles subject to section 280F are eligible for section 179 expensing only to the extent of the applicable limits contained in section 280F.		sport utility vehicle is defined to exclude any vehicle that: (1) is designed for more than nine individuals in seating rearward of the driver's seat; (2) is equipped with an open cargo area, or a covered box not readily accessible from the passenger compartment, of at least six feet in interior length; or (3) has an integral enclosure, fully enclosing the driver compartment and load carrying device, does not have seating rearward of the driver's seat, and has no body section protruding more than 30 inches ahead of the leading edge of the windshield. <u>Effective date</u>.–Property acquired after the date of enactment.
23. Consistent amortization of periods for intangibles (sec. 474 of the Senate amendment)	At the election of the taxpayer, start-up expenditures and organizational expenditures may be amortized over a period of not less than 60 months. Section 197 requires most acquired intangible assets (such as goodwill, trademarks, franchises, and	No provision.	Provides taxpayers an election to deduct up to $5,000 each of start-up and organizational expenditures in the taxable year in which the trade or business begins. However, each $5,000 amount is reduced (but not below zero) by the amount by which the cumulative cost of start-up or organizational expenditures

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	patents) that are held in connection with the conduct of a trade or business or an activity for the production of income to be amortized over 15 years.		exceeds $50,000, respectively. Start-up and organizational expenditures that are not deductible in the year in which the trade or business begins would be amortized over a 15-year period consistent with the amortization period for section 197 intangibles. <u>Effective date</u>.–Amounts incurred after date of enactment.
24. Doubling of certain penalties, fines, and interest on underpayments related to certain offshore financial arrangements (sec. 483 of the Senate amendment)	The Code contains numerous civil penalties, such as the delinquency, accuracy-related and fraud penalties. These civil penalties are in addition to any interest that may be due. In January 2003, Treasury announced the Offshore Voluntary Compliance Initiative ("OVCI") running through April 15, 2003, to encourage the voluntary disclosure of previously unreported income placed by taxpayers in offshore accounts and accessed through credit card or other financial arrangements. The taxpayer will pay back taxes, interest and certain accuracy-related and delinquency penalties.	No provision.	Increases by a factor of two the total amount of civil penalties, interest and fines applicable for taxpayers who would have been eligible to participate in either the OVCI or the Treasury Department's voluntary disclosure initiative but did not participate in either program. <u>Effective date</u>.–Taxpayers' open tax years on or after date of enactment.

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	A taxpayer's timely, voluntary disclosure of a substantial unreported tax liability has long been an important factor in deciding whether the taxpayer's case should ultimately be referred for criminal prosecution. The voluntary disclosure must be truthful, timely, and complete. A voluntary disclosure does not guarantee immunity from prosecution.		
25. Whistleblower reforms (sec. 488 of the Senate amendment)	Under section 7623, the IRS is authorized to pay such sums as deemed necessary for: "(1) detecting underpayments of tax; and (2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same." Amounts are paid based on a percentage of tax, fines, and penalties (but not interest) actually collected based on the information provided. For specific information that caused the investigation and resulted in recovery, the IRS administratively has set the reward in an amount not to exceed 15 percent of the amounts recovered. For information, although not specific, that nonetheless caused	No provision.	Creates a reward program for actions in which the tax, penalties, interest, additions to tax, and additional amounts in dispute exceed $20,000, and, if the taxpayer is an individual, the individual's gross income exceeds $200,000 for any taxable year. Generally, establishes a reward floor of 15 percent of the collected proceeds (including penalties, interest, additions to tax and additional amounts) if the IRS proceeds with an administrative or judicial action based on information brought to the IRS's attention by an individual. Permits awards of lesser amounts (but no less than 10 percent) if the action

Provision	Present Law	House Bill	Senate Amendment
	the investigation and was of value in the determination of tax liabilities, the reward is not to exceed 10 percent of the amount recovered. For information that caused the investigation, but had no direct relationship to the determination of tax liabilities, the reward is not to exceed one percent of the amount recovered. The reward ceiling is $10 million (for payments made after 11/7/2002), and the reward floor is $100. No reward will be paid if the recovery was so small as to call for payment of less than $100 under the above formulas. Both the ceiling and percentages can be increased with a Special Agreement. The Code permits the IRS to disclose return information pursuant to a contract for tax administration services (sec. 6103(n)).		was based principally on allegations (other than information provided by the individual) resulting from a judicial or administrative hearing, government report, hearing, audit, investigation, or from the news media. Caps the available reward at 30 percent of the collected proceeds. Any determination regarding a reward may be appealed to the U.S. Tax Court. Creates a Whistleblower Office within the IRS to administer this reward program. The Whistleblower Office is funded with amounts equal to rewards made. The Whistleblower Office may seek the assistance from the individual providing information or from his legal representative, and may reimburse the costs incurred by any legal representative out of the funds of the Whistleblower Office. To the extent the disclosure of returns or return information is required to render such assistance, the disclosure must be pursuant to an IRS tax administration contract.

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			Effective date.–Information provided on or after the date of enactment.
26. Increase in age of minor children whose unearned income is taxed as if parent's income (sec. 495 of the Senate amendment)	Certain unearned income of a child under age 14 is taxed at the parent's tax rate and by adding the child's net unearned income to the parent's taxable income. In limited circumstances a parent may elect to include the child's income on the parent's return, rather than file a separate return for the child.	No provision.	Increases the age at which income of a minor child is taxed as if it is income of the child's parent, from under 14 to under 18. Effective date.–Taxable years beginning after December 31, 2003.
27. Holding period for preferred stock (sec. 496 of Senate amendment)	For taxable years beginning before January 1, 2009, dividends received by an individual shareholder from domestic corporations and certain foreign corporations generally are taxed at the same rates that apply to net capital gain (i.e., 5 percent (zero percent for taxable years beginning after 2007) and 15 percent). To qualify, the shareholder must hold the dividend-paying stock for more than 60 days during the 120-day period beginning 60 days before the ex-dividend date (in the case of preferred stock, for more than 90 days during the 180-day period	No provision.	For preferred stock, extends the holding period requirement to require that the shareholder hold the dividend-paying stock for more than 120 days during the 240-day period beginning 120 days before the ex-dividend date (i.e., double the present-law required holding period for common stock). Effective date.–Taxable years beginning after the date of enactment.

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	beginning 90 days before the ex-dividend date).		
28. Grant Treasury regulatory authority to address foreign tax credit transactions involving inappropriate separation of foreign taxes from related foreign income (sec. 661A of the Senate amendment)	The United States provides a credit for foreign income taxes paid or accrued. For foreign tax credit purposes, the taxpayer "is the person on whom foreign law imposes legal liability for such tax." Treas. Reg. sec. 1.901-2(f)(1). Thus, if a U.S. corporation owns a foreign entity that is a partnership for foreign tax purposes, the U.S. corporation can claim foreign tax credits for the tax that is imposed on it as a partner in the foreign entity. This is true even if the U.S. corporation elects to treat the foreign entity as a corporation for U.S. tax purposes. If the foreign entity does not generate subpart F income, or if the foreign entity does not meet the definition of a CFC, the income generated by the foreign entity may never be reported on a U.S. return, despite the fact that the U.S. corporation can claim credits for taxes imposed on that income.	No provision.	Expands existing regulatory authority to provide Treasury and the IRS additional mechanisms to address the second class of transactions described in Notice 98-5 as well as other abusive foreign tax credit schemes that involve the inappropriate separation of foreign taxes from the related foreign income in cases where foreign taxes are imposed on any person with respect to income of an entity. The regulations may provide for: (1) the disallowance of a credit for all or a portion of the foreign taxes; or (2) for the allocation of the foreign taxes among the participants in the transaction in a manner that is more consistent with the underlying economics of the transaction. <u>Effective date</u>.–The provision is effective for transactions entered into after the date of enactment.

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29. Freeze of provision regarding suspension of interest where Secretary fails to contact taxpayer (sec. 662B of the Senate amendment)	In general, interest and penalties accrue during periods for which taxes were unpaid without regard to whether the taxpayer was aware that there was tax due. The Code suspends the accrual of certain penalties and interest for individuals after one year if the IRS has not sent the taxpayer a notice specifically stating the taxpayer's liability and the basis for the liability within the specified period. With respect to taxable years beginning before January 1, 2004, the one-year period is increased to 18 months.	No provision.	Makes the 18-month rule the permanent rule. Adds gross misstatements and listed and reportable transactions to the list of provisions to which the suspension of interest rules do not apply. <u>Effective date</u>.–Taxable years beginning after December 31, 2003, except addition of listed and reportable transactions applies to interest accruing after May 5, 2004.
30. Increase in withholding for supplemental wage payments in excess of $1 million (sec. 673 of the Senate amendment)	An employer must withhold income taxes from wages paid to employees. There are several possible methods for determining the amount of income tax to be withheld. The IRS publishes tables to be used in determining the amount of income tax to be withheld. In some cases, "supplemental" wage payments (e.g., bonuses or commissions) may be subject to withholding at a flat rate, based on the third lowest income tax rate under the Code (25 percent for 2004).	No provision.	Once annual supplemental wage payments to an employee exceed $1 million, any additional supplemental wage payments to the employee in that year are subject to withholding at the highest income tax rate (35 percent for 2004), regardless of any other withholding rules and regardless of the employee's Form W-4. <u>Effective date</u>.–Payments made after December 31, 2003.

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31. Treatment of sale of stock acquired pursuant to exercise of stock options to comply with conflict-of-interest requirements (sec. 674 of the Senate amendment)	If an employee disposes of stock acquired upon the exercise of a statutory stock option, the employee is taxed at capital gains rates with respect to the excess of the fair market value of the stock on the date of disposition over the option price unless the employee fails to meet the holding period requirement (two years after the date the option is granted or one year after the date the option is exercised). The gain upon a disposition that occurs prior to the expiration of the applicable holding period does not qualify for capital gains treatment.	No provision.	An eligible person who, in order to comply with Federal conflict of interest requirements, is required to sell shares of stock acquired pursuant to the exercise of a statutory stock option is treated as satisfying the statutory holding period requirements, regardless of how long the stock was actually held. Effective date.–Sales after the date of enactment.
32. Application of basis rules to employer and employee contributions on behalf of nonresident aliens (sec. 675 of the Senate amendment)	Basis in distributions from retirement plans includes amounts contributed by the participant on an after-tax basis, together with certain amounts contributed by the employer, minus the aggregate amount (if any) previously distributed to the extent that such amount was excludable from gross income. Amounts contributed by the employer are included in the calculation of the participant's basis only to the extent that such amounts were includible in the gross income of the participant, or	No provision.	Employee or employer contributions are not included in basis if: (1) the employee was a nonresident alien at the time the services were performed with respect to which the contribution was made; (2) the contribution is with respect to compensation for labor or personal services from sources without the United States; and (3) the contribution was not subject to income tax under the laws of the United States or any foreign country.

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	to the extent that such amounts would have been excludable from the participant's gross income if they had been paid directly to the participant at the time they were contributed. Employer contributions to retirement plans and other payments for labor or personal services performed outside the United States by nonresident aliens generally are not treated as U.S. source income. Such contributions, therefore, generally would not be includible in the nonresident alien's gross income if they had been paid directly to the nonresident alien at the time they were contributed. Thus, the amounts of such contributions generally are includible in the employee's basis and are not taxed by the United States if a distribution is made when the employee is a U.S. citizen or resident		<u>Effective date</u>.–Distributions on or after date of enactment.

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33. Substantial presence test required to determine bona fide residence in United States possession (sec. 497 of the Senate amendment)	An alien is considered a resident of the United States if the individual: (1) has entered the United States as a lawful permanent resident and is such a resident at any time during the calendar year; (2) is present in the United States for a substantial period of time (the so-called "substantial presence test"); or (3) makes an election to be treated as a resident of the United States (sec. 7701(b)). An alien who does not meet the definition of a "resident alien" is considered to be a non-resident alien for U.S. income tax purposes. Under the substantial presence test, an alien individual is generally treated as a resident alien if he or she is present in the United States for 31 days during the taxable year and the sum of the number of days on which such individual was present in the United States (when multiplied by the applicable multiplier) during the current year and the preceding two calendar years equals or exceeds 183 days. The applicable multiplier for: the current year is one, for the first	No provision.	Amends the current rules governing when an U.S. citizen or resident is treated as a bona fide resident of the Virgin Islands, Puerto Rico, Guam, Northern Mariana Islands, or American Samoa. U.S. citizens would only be treated as bona fide residents of these U.S. possessions for U.S. income tax purposes if they satisfy an objective, day counting test based on the substantial presence test. Provision also requires bona fide residents of the Virgin Islands to file an informational income tax return with the United States, and imposes a penalty for the failure to file such a return. <u>Effective date</u>.–The provision is effective for taxable years ending after the date of enactment.

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	preceding year is 1/3, and for the second preceding year is 1/6. Special income tax rules apply with respect to bona fide residents of certain U.S. possessions, including Virgin Islands, Puerto Rico, Guam, Northern Mariana Islands, and American Samoa. Generally, for U.S. citizens and residents, bona fide residence in a possession is determined using the principles of a subjective, facts-and-circumstances test set forth in regulations under section 871. However, for aliens, bona fide residence in a possession, which has a mirror code, is determined under the principles used to determine U.S. residence (discussed above).		
34. Include employer provided housing under foreign earned income exclusion cap (sec. 632(c) of the Senate amendment)	U.S. citizens living abroad may be eligible to exclude from their income for U.S. tax purposes: 1) foreign earned income; and 2) foreign housing costs. The combined earned income exclusion and housing cost exclusion may not exceed the	No provision.	Applies the annual foreign earned income exclusion cap ($80,000 for 2004) to the combined value of foreign earned income and employer-provided housing amounts. The present-law provision providing indexation for inflation for tax years beginning after 2007 would remain unchanged.

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	taxpayer's total foreign earned income for the taxable year. The exclusion for foreign earned income generally applies to income earned from sources outside the United States as compensation for personal services actually rendered by the taxpayer and the maximum exclusion for a taxable year is $80,000. For taxable years beginning after 2007, the maximum exclusion amount is indexed for inflation. The exclusion for housing costs applies to reasonable expenses paid or incurred by or on behalf of the taxpayer for housing. The exclusion amount for housing costs is equal to the excess of such housing costs over a base housing amount for the taxable year.		The present-law provision imposing an additional foreign earned income cap on exclusions and deductions would also remain unchanged. <u>Effective date</u>.–Taxable years beginning after December 31, 2003.
35. Limit deduction for certain entertainment expenses (including company-provided aircraft) for covered employees (sec. 103(b) of the Senate amendment)	No deduction is allowed with respect to (1) an activity generally considered to be entertainment, amusement or recreation, unless the taxpayer establishes that the item was directly related to (or, in certain cases, associated with) the active conduct of the taxpayer's trade or business, or (2) a facility	No provision.	In the case of covered employees (as defined in Code section 162(m)(3)), the exception to the general entertainment expense disallowance rule for expenses treated as compensation or includible in income applies only to the extent of the amount of

Provision	Present Law	House Bill	Senate Amendment
	used in connection with such activity. The deduction disallowance rule does not apply to expenses for goods, services, and facilities to the extent that the expenses are reported by the taxpayer as compensation and wages to an employee. In the context of an employer providing an aircraft to employees for nonbusiness (e.g., vacation) flights, this exception has been interpreted as not limiting the company's deduction for operation of the aircraft to the amount of compensation reportable to its employees. *Sutherland Lumber-Southwest, Inc. v. Comm.*, 114 T.C. 197 (2000), *aff'd*, 255 F.3d 495 (8th Cir. 2001).		expenses treated as compensation and wages. Effective date.–Expenses incurred after the date of enactment and before January 1, 2006.
36. Treatment of contingent payment convertible debt instruments (sec. 733 of the Senate amendment)	Taxpayers generally deduct interest paid or accrued within the taxable year on indebtedness issued by the taxpayer. In the case of original issue discount ("OID"), the issuer of a debt instrument generally accrues and deducts, as interest, the OID over the life of the obligation, even though the amount of the OID may not be paid until the maturity of the instrument. Treasury regulations provide special rules for determining the amount of OID	No provision.	Provides that, in the case of a contingent convertible debt instrument, any Treasury regulations which require OID to be determined by reference to the comparable yield of a noncontingent fixed-rate debt instrument shall be applied as requiring that such comparable yield be determined by reference to a noncontingent fixed-rate debt instrument which is convertible into stock. Also provides that the

Provision	Present Law	House Bill	Senate Amendment
	allocated to a period with respect to certain debt instruments that provide for one or more contingent payments of principal or interest. With respect to certain debt instruments that are convertible into stock of the issuer and that also provide for contingent payments ("contingent convertible" debt instruments), the IRS has stated that the special rules for contingent payment debt instruments apply in computing the accrual of OID on the debt instrument, and that the comparable yield for a contingent convertible debt instrument is determined by reference to a comparable fixed-rate nonconvertible debt instrument.		comparable yield shall be determined without taking into account the yield resulting from the conversion of a debt instrument into stock. Thus, the Treasury regulations shall be applied in a manner such that the comparable yield for contingent convertible debt instruments shall be determined by reference to comparable noncontingent fixed-rate convertible (rather than nonconvertible) debt instruments. <u>Effective date</u>.–Debt instruments issued after the date of enactment.