H.R. 4213
Tax Extenders Act of 2009

December 8, 2009

Summary: The *Tax Extenders Act of 2009* would provide individuals and businesses with approximately $31 billion in tax relief in 2009 by extending for one year (through 2010) more than forty provisions that are scheduled to expire at the end of 2009. This $31 billion in tax relief includes more than $5 billion in individual tax relief and more than $17 billion in business tax relief. The *Tax Extenders Act of 2009* also extends more than $7 billion of tax provisions that encourage charitable contributions, provide community development incentives, provide tax relief in the event of a Presidentially-declared disaster, and support the deployment of alternative vehicles and alternative fuels. The *Tax Extenders Act of 2009* provides this relief without adding to the deficit.

I. TRADITIONAL TAX EXTENDERS

a. INDIVIDUAL PROVISIONS

Extension of the deduction of State and local general sales taxes. The bill would extend for one year (through 2010) the election to take an itemized deduction for State and local general sales taxes in lieu of the itemized deduction permitted for State and local income taxes. *This proposal is estimated to cost $1.846 billion over 10 years*.

Extension of the additional standard deduction for real property taxes. The bill would extend for one year (through 2010) the additional standard deduction for State and local real property taxes. *This proposal is estimated to cost $1.460 billion over 10 years.*

Extension of the above-the-line deduction for qualified tuition and related expenses. The bill would extend for one year (through 2010) the above-the-line tax deduction for qualified education expenses. *This proposal is estimated to cost $1.529 billion over 10 years.*

Extension of the above-the-line deduction for certain expenses of elementary and secondary school teachers. The bill would extend for one year (through 2010) the $250 above-the-line tax deduction for teachers and other school professionals for expenses paid or incurred for books, supplies (other than non-athletic supplies for courses of instruction in health or physical education), computer equipment (including related software and service), other equipment, and supplementary materials used by the educator in the classroom. *This proposal is estimated to cost $228 million over 10 years.*

b. <u>BUSINESS PROVISIONS</u>

Extension of the R&D credit. The bill would extend for one year (through 2010) the research credit. *This proposal is estimated to cost $6.966 billion over 10 years.*

Extension of active financing exception. The bill would extend for one year (through 2010) the active financing exception from Subpart F of the tax code. *This proposal is estimated to cost $3.923 billion over 10 years.*

Extension of look-through treatment of payments between related controlled foreign corporations. The bill would extend for one year (through 2010) the current law look-through treatment of payments between related controlled foreign corporations. *This proposal is estimated to cost $574 million over 10 years*.

Extension of 15-year straight-line cost recovery for qualified leasehold improvements, restaurant buildings and improvements, and retail improvements. The bill would extend for one year (through 2010) the special 15-year cost recovery period for certain leasehold improvements, restaurant buildings and improvements, and retail improvements. *This proposal is estimated to cost $5.390 billion over 10 years.*

Extension of 7-year straight line cost recovery period for motorsports entertainment complexes. The bill would extend for one year (through 2010) the special 7-year cost recovery period for property used for land improvement and support facilities at motorsports entertainment complexes. *This proposal is estimated to cost $45 million over 10 years*.

Extension of railroad track maintenance credit. The bill would extend for one year (through 2010) the railroad track maintenance credit. *This proposal is estimated to cost $165 million over 10 years.*

Extension of special expensing rules for U.S. film and television productions. The bill would extend for one year (through 2010) the provision that allows film and television producers to expense the first $15 million of production costs incurred in the United States ($20 million if the costs are incurred in economically depressed areas in the United States). *This proposal is estimated to cost $51 million over 10 years.*

Extension of expensing of "brownfields" environmental remediation costs. The bill would extend for one year (through 2010) the provision that allows for the expensing of costs associated with cleaning up hazardous ("brownfield") sites. *This proposal is estimated to cost $159 million over 10 years.*

Extension of mine rescue team training credit. The bill would extend for one year (through 2010) the credit for training mine rescue team members. *This proposal is estimated to cost $1 million over 10 years.*

Extension of election to expense advanced mine safety equipment. The bill would extend for one year (through 2010) the provision that provides businesses with fifty percent (50%) bonus depreciation for certain qualified underground mine safety equipment. *This proposal is estimated to cost $5 million over 10 years.*

Extension of employer wage credit for activated military reservists. The bill would extend for one year (through 2010) the provision that provides eligible small business employers with a credit against the taxpayer's income tax liability for a taxable year in an amount equal to twenty percent (20%) of the sum of differential wage payments to activated military reservists. *This proposal is estimated to cost $4 million over 10 years.*

Extension of five-year depreciation for farming business machinery and equipment. The bill would extend for one year (through 2010) the provision that provides a five-year recovery period for certain machinery and equipment which is used in a farming business. *This proposal is revenue neutral over 10 years.*

Extension of special rules for regulated investment companies. The bill would extend for one year (through 2010) the tax treatment of interest-related dividends, short-term capital gain dividends, and other special rules applicable to foreign shareholders that invest in regulated investment companies. *These proposals are estimated to cost $94 million over 10 years.*

Extension of special rule for percentage depletion for marginal wells. The bill would extend for one year (through 2010) the suspension on the taxable income limit for purposes of depleting a marginal oil or gas well. *This proposal is estimated to cost $104 million over 10 years.*

c. CHARITABLE PROVISIONS

Extension of provision encouraging contributions of capital gain real property for conservation purposes. The bill would extend for one year (through 2010) the increased contribution limits and carryforward period for contributions of appreciated real property (including partial interests in real property) for conservation purposes. *This proposal is estimated to cost $182 million over 10 years.*

Extension of enhanced charitable deduction for contributions of food inventory. The bill would extend for one year (through 2010) the provision allowing businesses to claim an enhanced deduction for the contribution of food inventory. *This proposal is estimated to cost $78 million over 10 years.*

Extension of enhanced charitable deduction for contributions of book inventories to public schools. The bill would extend for one year (through 2010) the provision allowing C corporations to claim an enhanced deduction for contributions of book inventory to public schools (kindergarten through grade 12). *This proposal is estimated to cost $31 million over 10 years.*

Extension of enhanced charitable deduction for corporate contributions of computer equipment for educational purposes. The bill would extend for one year (through 2010) the provision that encourages businesses to contribute computer equipment and software to elementary, secondary, and post-secondary schools by allowing an enhanced deduction for such contributions. *This proposal is estimated to cost $195 million over 10 years.*

Extension of tax-free distributions from individual retirement plans for charitable purposes. The bill would extend for one year (through 2010) the provision that permits tax-free distributions to charity from an Individual Retirement Account (IRA) of up to $100,000 per taxpayer, per taxable year. *This proposal is estimated to cost $591 million over 10 years*.

Extension of special tax treatment of certain payments to controlling exempt organizations. The bill would extend for one year (through 2010) the special rules for interest, rents, royalties and annuities received by a tax exempt entity from a controlled entity. *This proposal is estimated to cost $20 million over 10 years.*

Extension of exclusion of gain on the sale or exchange of certain brownfield sites from unrelated business taxable income. The bill would extend for one year (through 2010) the provision that excludes any gain or loss from the qualified sale, exchange, or other disposition of any qualified brownfield property from unrelated business taxable income. *This proposal is estimated to cost $47 million over 10 years*.

Extension of special rule for S corporations making charitable contributions of property. The bill would extend for one year (through 2010) the provision allowing S corporation shareholders to take into account their pro rata share of charitable deductions even if such deductions would exceed such shareholder's adjusted basis in the S corporation. *This proposal is estimated to cost $37 million over 10 years.*

d. MISCELLANEOUS PROVISIONS

Extension of Indian employment credit. The bill would extend for one year (through 2010) the business tax credit for employers of qualified employees that work and live on or near an Indian reservation. The credit is for wages and health insurance costs paid to qualified employees (up to $20,000) in the current year over the amount paid in 1993. *This proposal is estimated to cost $49 million over 10 years.*

Extension of accelerated depreciation for business property on an Indian reservation. The bill would extend for one year (through 2010) the placed-in-service date for the special depreciation recovery period for qualified Indian reservation property. In general, qualified Indian reservation property is property used predominantly in the active conduct of a trade or business within an Indian reservation, which is not used outside the reservation on a regular basis and was not acquired from a related person. *This proposal is estimated to cost $125 million over 10 years.*

Extension of deduction allowable with respect to income attributable to domestic production activities in Puerto Rico. The bill would extend for one year (through 2010) the provision extending the section 199 domestic production activities deduction to activities in Puerto Rico. *This proposal is estimated to cost $185 million over 10 years.*

Extension of temporary increase in limit on cover over of rum excise tax revenues to Puerto Rico and the Virgin Islands. The bill would extend for one year (through 2010) the provision providing for payment of $13.25 per gallon to cover over a $13.50 per proof gallon excise tax on distilled spirits produced in or imported into the United States. *This proposal is estimated to cost $128 million over 10 years.*

Extension of American Samoa economic development credit. The bill would extend for one year (through 2010) the American Samoa economic development credit. In general, this credit provides certain domestic corporations operating in American Samoa with a possessions tax credit to offset their U.S. tax liability on income earned in American Samoa from active business operations, sales of assets used in a business, or certain investments in American Samoa. *This proposal is estimated to cost $18 million over 10 years.*

II. EXPIRING COMMUNITY ASSISTANCE PROGRAMS

Extension of tax incentives for Empowerment Zones. The bill would extend for one year (through 2010) the designation of certain economically depressed census tracts as Empowerment Zones. Businesses and individual residents within Empowerment Zones are eligible for special tax incentives. *This proposal is estimated to cost $381 million over 10 years.*

Extension of tax incentives for Renewal Communities. The bill would extend for one year (through 2010) the designation of certain economically depressed census tracts as Renewal Communities. Businesses and individual residents within Renewal Communities are eligible for special tax incentives. *This proposal is estimated to cost $786 million over 10 years.*

New markets tax credit. The bill would extend for one year (through 2011) the new markets tax credit, permitting a maximum annual amount of qualified equity investments of $5 billion. *This proposal is estimated to cost $1.402 billion over 10 years.*

Extension of tax incentives for the District of Columbia. The bill would extend for one year (through 2010) the designation of certain economically depressed census tracts within the District of Columbia as the District of Columbia Enterprise Zone. Businesses and individual residents within this enterprise zone are eligible for special tax incentives. The bill would also extend for one year (through 2010) the $5,000 first-time homebuyer credit for the District of Columbia. *This proposal is estimated to cost $17 million over 10 years*.

Extension of tax incentives for the New York Liberty Zone. The bill would extend for one year (through 2010) the special depreciation allowance for certain real property within the New York Liberty Zone and the time for issuing New York Liberty Zone bonds. *This proposal is estimated to cost $318 million over 10 years.*

Extend Work Opportunity Tax Credit (WOTC) for Hurricane Katrina Employees. The bill would extend for one year (through August 28, 2010) the work opportunity tax credit for certain employers hiring in the Hurricane Katrina core disaster area. *This proposal is estimated to cost $7 million over 10 years.*

Extension of Increased Rehabilitation Credit for Historic Structures in the Gulf Opportunity Zone. The bill would extend for one year (through 2010) the increased rehabilitation credit for qualified expenditures in the Gulf Opportunity Zone. The Gulf

Opportunity Zone Act of 2005 increased the rehabilitation credit from 10 percent to 13 percent of qualified expenditures for any qualified rehabilitated building other than a certified historic structure, and from 20 percent to 26 percent of qualified expenditures for any certified historic structure. *This proposal is estimated to cost $25 million over 10 years.*

Election for refundable low-income housing credit for 2010. The bill would extend for one year (through 2010) the program that was enacted as part of the *American Recovery and Reinvestment Act of 2009* that allows state housing agencies to elect to receive a payment in lieu of a portion of the State's allocation of low-income housing tax credits. *This proposal is estimated to cost $471 million over 10 years.*

III. EXPIRING GENERAL DISASTER TAX RELIEF PROVISIONS

Extension of expanded and enhanced casualty loss deductions relating to federal disasters. The bill would extend for one year (through 2010) the provision that allows taxpayers who have suffered loss as a result of a Federally-declared disaster to claim a deduction for casualty losses (i.e., both itemizers and non-itemizers) and would allow these taxpayers to calculate their casualty loss deduction without regard to their adjusted gross income. The bill would also extend for one year (through 2010) the current law $500 per loss threshold. *This proposal is estimated to cost $728 million over 10 years.*

Extension of expensing of qualified disaster expenses. The bill would extend for one year (through 2010) the provision that allows businesses hat have been affected by a Federally-declared disaster to currently deduct demolition, repair, clean-up, and environmental remediation expenses ("Qualified Disaster Expenses"). *This proposal is estimated to cost $32 million over 10 years.*

Extension of five-year carry-back period for certain losses relating to federal disasters. The bill would extend for one year (through 2010) the provision that allows businesses to carry back to the previous five years the following losses: (1) casualty losses that are attributable to a Federally-declared disaster; and (2) Qualified Disaster Expenses. *This proposal is estimated to cost $129 million over 10 years.*

Extension of relaxed mortgage revenue bond limitations for federal disasters. The bill would extend for one year (through 2010) the provision that allows states waive certain rules that limit their ability to use tax-exempt housing bonds to provide loans to taxpayers that wish to acquire residences in Federally-declared disaster areas. The bill would also extend for one year (through 2010) the provision that allows states to use their tax-exempt housing bonds to provide loans to repair or reconstruct homes and rental housing units that have been rendered unsafe for use as a residence by reason of a Federally-declared disaster or have been demolished or relocated by reason of government order on account of a Federally-declared disaster. Such loans are limited to the lower of (1) the actual cost of the repair or reconstruction or (2) $150,000. *This proposal is estimated to cost $63 million over 10 years.*

Extension of bonus depreciation for qualified disaster property. The bill would extend for one year (through 2010) the provision that permits businesses that suffered damage as a result of a Federally-declared disaster to claim an additional first-year depreciation deduction equal to 50 percent of the cost of new real and personal property investments made in the Presidentially-declared disaster area. *This proposal is estimated to cost $1.434 billion over 10 years.*

Extension of increased small business expensing for expenditures relating to federal disasters. The bill would extend for one year (through 2010) the provision that increases by $100,000 (or the cost of qualified property, if less) the amount of expensing available for qualifying expenditures made in a Federally-declared disaster area. The bill would also extend for one year (through 2010) the provision that increases by $600,000 (or the cost of qualified property, if less) the level of investment at which the small business expensing benefits phase-out. *This proposal is estimated to cost $1 million over 10 years.*

IV. EXPIRING ENERGY TAX PROVISIONS

Extension of tax incentives for biodiesel and renewable diesel. The bill would extend for one year (through 2010) the $1.00 per gallon production tax credit for biodiesel and the small agri-biodiesel producer credit of 10 cents per gallon. The bill would also extend for one year (through 2010) the $1.00 per gallon production tax credit for diesel fuel created from biomass. *This proposal is estimated to cost $1.008 billion over 10 years.*

Extension of the alternative motor vehicle credit for heavy hybrids. The bill would extend for one year (through 2010) the alternative motor vehicle credit for so-called heavy hybrids (i.e., hybrid motor vehicles that are not passenger automobiles or light trucks). *This proposal is estimated to cost $7 million over 10 years.*

Extension of tax incentive for natural gas and propane used as a fuel in transportation vehicles. The bill would extend for one year (through 2010) the $0.50 per gallon production tax credit for natural gas and propane used as a transportation fuel. The bill would not extend this credit for propane used to power forklifts. *This proposal is estimated to cost $125 million over 10 years.*

Extension of special rule for sales of electric transmission property. The bill would extend for one year (for sales prior to January 1, 2011) the present law deferral of gain on sales of transmission property by vertically integrated electric utilities to FERC-approved independent transmission companies. Rather than recognizing the full amount of gain in the year of sale, this provision would allow gain on such sales to be recognized ratably over an eight-year period. *This proposal is revenue neutral over 10 years.*

V. REVENUE PROVISIONS

a. FOREIGN ACCOUNT TAX COMPLIANCE ACT OF 2009 (H.R. 3933 & S.1934)

Summary: Recent events have highlighted the growing use of foreign financial institutions, foreign trusts, and foreign corporations by U.S. individuals to evade U.S. tax. In order to prevent this tax evasion, the *Foreign Account Tax Compliance Act of 2009* would provide the U.S.

Treasury Department with significant new tools to find and prosecute U.S. individuals that hide assets overseas from the Internal Revenue Service.

Based on proposals included in President Obama's 2010 Budget, on legislation proposed by Senator Carl Levin and Representative Lloyd Doggett, and a draft released by Senator Max Baucus, the *Foreign Account Tax Compliance Act* would force foreign financial institutions, foreign trusts, and foreign corporations to provide information about their U.S. accountholders, grantors, and owners, respectively. The nonpartisan Joint Committee on Taxation has estimated the provisions of the *Foreign Account Tax Compliance Act* would prevent U.S. individuals from evading $7.7 billion in U.S. tax over the next ten years.

The Foreign Account Tax Compliance Act of 2009 has been developed in close consultation with the U.S. Department of the Treasury, and is the legislative product of numerous hearings conducted in the Senate Permanent Select Committee on Investigations, the Select Revenue Measures Subcommittee of the House Ways and Means Committee, and the Senate Finance Committee.

INCREASED DISCLOSURE OF BENEFICIAL OWNERS

Reporting on certain foreign bank accounts. As a tax enforcement tool, the United States requires U.S. financial institutions to file annual information returns disclosing and reporting on the activities of bank accounts held by U.S. individuals. Many U.S. individuals looking to evade their tax obligations in the United States have sought to hide income and assets from the Internal Revenue Service ("IRS") by opening secret foreign bank accounts with foreign financial institutions. Some foreign financial institutions have voluntarily agreed to provide information on the U.S.-source income of U.S. accountholders as part of the "Qualified Intermediary" program since 2000. However, many of the foreign financial institutions that hold accounts on behalf of U.S. persons are outside the reach of U.S. law. As a result, the ability of the United States to require foreign financial institutions to disclose and report on U.S. accountholders is significantly limited. Although these foreign financial institutions are outside the direct reach of U.S. law, many of them have substantial investments in U.S. financial assets or hold substantial U.S. financial assets for the account of others.

The bill would impose a thirty percent (30%) withholding tax on certain income from U.S. financial assets held by a foreign financial institution unless the foreign financial institution agrees to disclose the identity of any U.S. individual with an account at the institution (or the institution's affiliates) and to annually report on the account balance, gross receipts and gross withdrawals/payments from such account. Foreign financial institutions would also be required to agree to disclose and report on foreign entities that have substantial U.S. owners. These disclosure and reporting requirements would be in addition to any requirements imposed under the Qualified Intermediary program. It is expected that foreign financial institutions would comply with these disclosure and reporting requirements in order to avoid paying this withholding tax.

Reporting on owners of foreign corporations, foreign partnerships and foreign trusts. Under present law, withholding agents are not required to look-through many foreign entities to determine whether such entity is owned by a U.S. individual. This aspect of present law has allowed U.S. individuals to evade their tax obligations in the United States by setting up foreign shell corporations, partnerships and trusts and investing overseas through these shell entities. The bill would require foreign entities to provide withholding agents with the name, address and tax identification number of any U.S. individual that is a substantial owner of the foreign entity (i.e., owns more than ten percent (10%) of the foreign corporation's stock (by vote or value), more than 10% of the profits or capital interest of a foreign partnership, or is treated as a grantor or holds more than 10% of the beneficial interest in a foreign trust). Withholding agents would report this information to the U.S. Treasury Department. The bill would exempt publicly-held and certain other foreign corporations from these reporting requirements and would provide the Treasury Department with the regulatory authority to exclude other recipients that pose a low risk of tax evasion. Any withholding agent making a withholdable payment to a foreign entity that does not comply with these disclosure and reporting requirements would be required to withhold tax at a rate of thirty percent (30%).

Extending bearer bond tax sanction to bearer bonds designed for foreign markets. Bearer bonds (i.e., bonds that do not have an official record of ownership) allow individuals seeking to evade taxes with the ability to invest anonymously. Recognizing the potential for U.S. individuals to take advantage of bearer bonds to avoid U.S. taxes, President Reagan and Congress took a number of steps in 1982 to eliminate bearer bonds in the United States. First, they prevented the United States government from issuing bearer bonds that would be marketed to U.S. investors. Second, they imposed sanctions on issuers of bearer bonds that could be purchased by U.S. investors. Under these sanctions, the issuer of such a bearer bond is not allowed to claim any interest deductions on the bond, the earnings and profits of a corporation are generally not reduced by the amount of any interest on the bond, and interest on the bond will not qualify for any applicable tax exemption (e.g., tax-exempt municipal bonds). Furthermore, certain issuers of such bearer bonds are also subject to an excise tax equal to one percent (1%) of the principal amount of the bearer bond multiplied by the term of the bond. If the issuer of the bearer bond is not subject to the excise tax, then the holder of the bearer bond would be subject to additional sanctions that apply when the bearer bond is sold, exchanged, lost or becomes worthless: (1) the loss of capital gains treatment and (2) the denial of loss deductions. Because the United States is asking other countries to eliminate opportunities for U.S. investors to purchase bearer bonds issued outside the United States, the bill would extend these sanctions (other than the excise tax) to bearer bonds that are marketed to foreign investors and would prevent the United States government from issuing any bearer bonds.

FOREIGN FINANCIAL ASSET REPORTING

Disclosure of information with respect to foreign financial assets. The bill would require any individual that holds more than $50,000 (in the aggregate) in (1) a depository or custodial account maintained by a foreign financial institution or (2) any foreign stock, interest in a foreign entity, or financial instrument with a foreign counterparty not held in a custodial account of a financial institution (collectively, "reportable foreign assets") to report information about these accounts and/or assets to the U.S. Treasury Department with the individual's annual tax return. Failures to comply with this requirement would be subject to a penalty of $10,000, and higher penalties (up to $50,000) could apply if the failure is not remedied within 90 days following notification from the Treasury Department.

Penalties for underpayments attributable to undisclosed foreign financial assets. The bill would impose a penalty equal to forty percent (40%) of the amount of any understatement that is attributable to an undisclosed foreign financial asset (i.e., any foreign financial asset that a taxpayer is required to disclose and fails to disclose on an information return).

Modification of statute of limitations for significant underreporting of income in connection with foreign assets. Under present law, additional Federal tax liabilities in the form of tax, interest, and penalties must be assessed by the Internal Revenue Service within three years after the date a return is filed. If an assessment is not made within the required time period, the additional liabilities generally cannot be assessed or collected at any future time. This three-year statute of limitations is extended to six years where there is a substantial omission of items from a tax return. This additional time gives the Internal Revenue Service an opportunity to identify the omission and determine the taxpayer's correct tax liability. In particular, it is often difficult for the Internal Revenue Service to identify omissions that arise in connection with foreign assets. However, the extended six-year statute of limitations only applies where the omission is in excess of twenty-five percent (25%) of the gross income stated on the tax return. The bill would extend the six-year statute of limitations for omissions that exceed $5,000 and are attributable to one or more reportable foreign assets. The bill would also clarify that the statute of limitations does not begin to run until the taxpayer files the information return disclosing the taxpayer's reportable foreign assets.

OTHER DISCLOSURE PROVISIONS

Passive foreign investment company reporting. Under present law, a shareholder of a passive foreign investment company (a "PFIC") is not required to file an information return with the Internal Revenue Service unless the shareholder recognizes gain on the sale of PFIC stock, receives a distribution from a PFIC, or the PFIC has filed a qualified electing fund ("QEF") election. The bill would require each person who is a shareholder of a passive foreign investment company to file an annual report containing such information as the Secretary may require.

E-Filing of Certain Financial Institution Returns. Under present law, the Treasury Department cannot require any person to file an electronic return unless such person is required to file at least 250 returns during the calendar year. The bill would provide an exception to this rule for financial institutions with respect to returns relating to withholding taxes. Under the bill, the Treasury Department may require financial institutions to file an electronic return even if such person would file fewer than 250 returns during the calendar year.

PROVISIONS RELATED TO FOREIGN TRUSTS

Clarifications with respect to foreign trusts. Under present law, a U.S. person is treated as the owner of the property transferred to a foreign trust if the trust has a U.S. beneficiary. Under current Treasury regulations, a foreign trust is treated as having a U.S. beneficiary if any current, future or contingent beneficiary of the trust is a U.S. person. Notwithstanding this requirement, some taxpayers have taken positions that are contrary to this regulation. In order to enhance compliance with this regulation, the bill would codify this regulation into the statute. The bill would also clarify that a foreign trust will be treated as having a U.S. beneficiary if (1) any person has discretion to determine the beneficiaries of the trust unless the terms of the trust specifically identify the class of beneficiaries and none of those beneficiaries are U.S. persons or (2) any written, oral or other agreement could result in a beneficiary of the trust being a U.S. person. As a final clarification, the bill would clarify that the use of any trust property will be treated as a payment from the trust in the amount of the fair market value of such use.

Presumption with respect to transfers to foreign trusts. The bill would provide that if a U.S. person directly or indirectly transfers property to a foreign trust (other than a trust established for deferred compensation or a charitable trust) the Secretary may treat the trust as having a U.S. beneficiary unless such person can demonstrate to the satisfaction of the IRS that under the terms of the trust, (1) no part of the trust may be paid or accumulated during the year for the benefit of a U.S. person, (2) that if the trust were terminated during the year, no part of the trust could be paid to a U.S. person, (3) and that such person provides any additional information as the Secretary of the Treasury may require with respect to such transfer.

Minimum penalty with respect to failure to report on certain foreign trusts. Under present law, a taxpayer that fails to file an information return with respect to certain transactions involving foreign trusts (e.g., the creation of a foreign trust, the transfer of money or property to a foreign trust, or the death of a U.S. owner of a foreign trust) is subject to a penalty of thirty-five percent (35%) of the amount required to be disclosed on such return. If the IRS uncovers the existence of an undisclosed foreign trust but is unable to determine the amount required to be disclosed on such return, it is unable to impose a penalty under present law. The bill would strengthen this penalty by imposing a minimum penalty of $10,000 on any such failure to file. Notwithstanding this minimum penalty, in no event would the penalties imposed on taxpayers for failing to file an information return with respect to a foreign trust exceed the amount required to be disclosed on such return.

DIVIDEND EQUIVALENT PAYMENTS

Treatment of substitute dividend payments and dividend equivalent payments received by foreign corporations in the same manner as dividends. Under present law, dividend payments made to foreign investors are subject to withholding tax at a rate of thirty percent (30%) unless otherwise reduced by an applicable tax treaty. In order to avoid this withholding tax, foreign investors have entered into transactions that provide them with substitute dividend payments and derivative transactions that provide them with dividend equivalent payments that are not subject to withholding. The bill would require withholding on substitute dividend payments and any dividend equivalent payments that are included in notional principal contracts (e.g., total return swap agreements) and would authorize the Treasury Department to develop rules that would require withholding on substitute dividends and dividend equivalent payments that are included in other financial arrangements.

a. CARRIED INTEREST

Taxation of carried interest as ordinary income. The bill would prevent investment fund managers from paying taxes at capital gains rates on investment management services income received as carried interest in an investment fund. The bill would require such managers to treat carried interest as ordinary income received in exchange for the performance of services to the extent that carried interest does not reflect a reasonable return on invested capital. The bill would continue to tax carried interest at capital gain tax rates to the extent that carried interest reflects a reasonable return on invested capital. This is consistent with the proposal to change the tax treatment of carried interest that is included in the President's FY2010 Budget. This provision has previously passed the House of Representatives on two occasions: first, as part of H.R. 3996 (110^{th} Congress) where it passed by a vote of 216 to 193; and second, as part of H.R. 6275 (110^{th} Congress) where it passed by a vote of 233 to 189 (with 10 Republicans joining with 223 Democrats in support). *This proposal is estimated to raise $24.616 billion over 10 years.*

VI. STUDY

Study of extended tax expenditures. The bill would direct the Chief of Staff of the Joint Committee on Taxation to submit a report to the Committee on Ways and Means and the Committee on Finance on each tax expenditure extended by this Act. *This proposal has no revenue effect.*