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Bailout Bill Tax Provisions – An Executive Summary

October 2008

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On Friday, October 3, the House passed H.R. 1424, the 'Emergency Economic Stabilization Act of 2008,' a controversial piece of legislation that authorizes a $700 billion financial bailout package. The legislation, previously passed by the Senate on October 1, was immediately signed into law by the President, also on October 3. Attached to the legislation was a package of tax extenders, one year of alternative minimum tax relief, disaster tax relief and energy tax incentives. The legislation gives the United States Treasury authority to establish a Troubled Assets Relief Program ("TARP") to purchase up to $700 billion in troubled assets from financial institutions with significant U.S. operations. Many of the tax provisions included in the legislation were contained in proposed legislation previously considered by Congress this year. Among the more significant business-related tax provisions are the following:[1]

1. Gain or loss realized by banks, savings and loan associations and certain other specified financial institutions on Fannie Mae or Freddie Mac preferred stock held on September 6, 2008 or sold or exchanged on or after January 1, 2008 and before September 7, 2008 will be treated as ordinary rather than capital gain or loss;
2. New limitations are imposed on tax deductions by financial institutions that participate in TARP for certain executive compensation payments and "golden parachute payments";
3. The current exclusion from taxable income of the first $2 million of discharge of mortgage debt relating to a taxpayer's primary residence is extended through the end of 2012;
4. The 30% investment tax credit for solar energy property and qualified fuel cell property, and the 10% investment tax credit for microturbines, are extended through 2016;
5. The placed-in-service date for claiming the production tax credit for electricity produced from qualified energy resources is extended, in the case of wind and refined coal facilities, through December 31, 2009, and through December 31, 2010 in the case of other energy sources;
6. New reporting rules are established effective January 1, 2011 (or later in the case of certain specified securities) requiring the reporting of customers' tax basis to the IRS by brokers for transactions involving securities such as stock, debt, commodities and derivatives and whether any resulting gain is long-term or short-term;
7. The credit for qualified research expenses that expired December 21, 2007 is extended for amounts paid or incurred before December 31, 2009. The alternative incremental research credit is eliminated for taxable years beginning after December 31, 2008, and the alternative simplified research credit rate is increased to 14% for 2009;
8. The "active financing income" exception from Subpart F income for earnings of a "controlled foreign corporation" engaged in an active banking, financing or similar business is extended to the end of 2009;
9. The look-through rule permitting deferral of income on certain dividend, interest, rent, and royalty payments received by one "controlled foreign corporation" from a related controlled foreign corporation is extended to the end of 2009;
10. The standards under Section 6694 with respect to the imposition of a penalty on the understatement of a taxpayer's liability by a tax return preparer are amended to conform to the standards imposed on the taxpayer;
11. The provision under current law which permits "regulated investment companies," under certain circumstances, to designate all or a portion of a dividend as an "interest-related dividend" is extended to the end of 2009 (interest-related dividends received by non-U.S. persons generally are not subject to U.S. gross-basis taxation);
12. The estate tax provision permitting a "look through" (in determining whether property of a decedent is treated as property within the United States) in the case of stock held by a

decedent in a regulated investment company is extended to apply to non-resident non-citizens dying after December 31, 2007 and before January 1, 2010;

13. The inclusion of regulated investment companies as "qualified investment entities" for purposes of determining whether a distribution received by a non-United States person is treated as gain from the sale of United States real property interests subject to tax under the FIRPTA provisions has been extended through December 31, 2009; and
14. Individuals (such as hedge fund managers) that are compensated under deferred compensation programs of certain "tax indifferent parties" (such as hedge funds operating in a low or no-tax jurisdiction) will be required to currently include such compensation in income.

Footnotes:

[1] The first three tax provisions described herein were passed into law as part of Emergency Economic Stabilization Act of 2008, the base legislation previously considered and rejected by the House. The next three provisions were included in the "Energy Improvement and Extension Act of 2008" and the remainder were part of the "Tax Extenders and Alternative Minimum Tax Relief Act of 2008." The Energy Improvement and Extension Act of 2008 and the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 were previously considered by the Senate and, on October 1, attached to the Emergency Economic Stabilization Act of 2008 and sent to the House for consideration as an integrated package.