

**COMPARISON OF PRINCIPAL HOUSE AND SENATE
NONQUALIFIED DEFERRED COMPENSATION PROPOSALS***

	H.R. 4520, The American Jobs Creation Act of 2004	S. 1637, Jumpstart Our Business Strength Act of 2004
In General	New Internal Revenue Code ("Code") section 409A provides that amounts deferred under a nonqualified deferred compensation plan (including earnings) are taxed immediately (except to the extent subject to a substantial risk of forfeiture) unless certain requirements are satisfied. Interest at the underpayment rate plus one percent is imposed on the underpayments that would have occurred had the compensation been taxable when first deferred or, if later, when not subject to a substantial risk of forfeiture.	New Code section 409A provides that amounts deferred under a nonqualified deferred compensation plan (including earnings) are taxed immediately (except to the extent subject to a substantial risk of forfeiture) unless certain requirements are satisfied. Interest at the underpayment rate is imposed on the underpayments that would have occurred had the compensation been taxable when first deferred or, if later, when not subject to a substantial risk of forfeiture. An additional ten percent penalty tax applies to amounts required to be included in income.
Definition of Nonqualified Deferred Compensation	Any plan or arrangement that provides for the deferral of compensation (whether voluntary or not), including nonqualified defined benefit plans (<u>i.e.</u> , "SERPs"). Exceptions are provided for "qualified employer plans"	Same, except that the proposed amendments do not apply to any nonelective deferred compensation attributable to services performed by non-employees to which Code section 457 does not apply by reason of Code section

* On October 28, 2003, the House Ways and Means Committee approved corporate and international tax reform legislation (H.R. 2896, the "American Jobs Creation Act of 2003") that contains a series of amendments to change the nonqualified deferred compensation rules. A similar, but more far-reaching, set of nonqualified deferred compensation amendments was included as part of Enron-related pension reform legislation (the "National Employee Savings and Trust Equity Guarantee Act of 2003" or "NESTEG") approved by the Senate Finance Committee on September 17, 2003 (and modified on February 2, 2004). A slightly modified version of the nonqualified deferred compensation amendments in NESTEG was added to the Senate version of corporate and international tax reform legislation (S. 1637, the "Jumpstart Our Business Strength (JOBS) Act of 2004") during floor debate on the bill. The Senate passed S. 1637 by a vote of 92-5 on May 11, 2004. The Ways and Means Committee approved a new version of corporate and international tax reform legislation (H.R. 4520, the "American Jobs Creation Act of 2004") on June 14, 2004, including a slightly modified version of the nonqualified deferred compensation amendments in H.R. 2896. The House passed H.R. 4520 by a vote of 251-178 on June 17, 2004.

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	or any bona fide vacation leave, sick leave, compensatory time, disability pay, or death benefit plan (with no exception for, e.g., severance plans, short-term deferrals, stock options, restricted stock, restricted stock units, or SARs). "Qualified employer plans" are a tax-qualified plan, tax-deferred annuity, SEP, SIMPLE, or governmental 457(b) plan. (Tax-exempt 457(b) and 457(f) plans would be subject to the proposed amendments).	457(e)(12), to the extent such deferred compensation is provided under a plan in existence on May 1, 2004.
Individuals Affected	In general, all individuals are subject to the new rules (not just individuals subject to sec. 16 of the Securities Act of '34 or who would be subject to sec. 16 if they were employed by a public company). Special distribution restrictions (described below) apply to key employees (defined in IRC sec. 416) of public companies upon a separation from service.	Generally the same. Special distribution restrictions (described below) apply to key employees (defined in IRC sec. 416) of public companies upon a separation from service and to individuals subject to sec. 16 of the Securities Act of '34 upon a change in control.
Restrictions on Distributions	<ul style="list-style-type: none"> • Distributions are permitted only upon: <ul style="list-style-type: none"> ▪ Separation from service (as determined by Treasury), ▪ death, ▪ disability, if the individual is either (1) disabled within the meaning of the Social Security Act, or (2) by reason of a medically determinable physical or mental impairment which can be expected to result in death or last for a continuous period of at least 12 months, receiving income replacement benefits for a period of at least 3 months under an accident and health plan covering the employees of the employer, ▪ a specified time (or pursuant to a fixed schedule), ▪ a change in ownership or effective control of the 	Generally the same. In the case of a participant subject to sec. 16 of the Securities Act of '34, distributions upon a change of control could not be made earlier than one year after the date of the change in control. Distributions made to such participants during the one-year period following a change in control (except by reason of death or disability) are treated as excess parachute payments under IRC sec. 280G and subject to the 20 percent excise tax under IRC sec. 4999. Coordination rules apply for purposes of applying the golden parachute and excise tax rules to other payments.

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	<p>corporation, or in the ownership of a substantial portion of the assets of the corporation, to the extent provided in Treasury regulations (under similar, but more restrictive, standards to the golden parachute rules in Code section 280G), and</p> <ul style="list-style-type: none"> ▪ an unforeseeable emergency (under standards similar to the "unforeseeable emergency" requirements in the final Code section 457 regulations). • Except as provided by Treasury in regulations, the acceleration of payments before the specified time or schedule chosen at the time of deferral is prohibited (which would eliminate the use of so-called "haircut" provisions). • Payments to "key employees" (as defined under the IRC section 416(i) top-heavy rules, which would include up to 50 officers) of a publicly traded corporation may not be made in the first six months following the individual's separation from service. 	
Restrictions on Timing of Deferrals	<p>Initial deferral elections are required to be made before the beginning of the taxable year in which the services are performed giving rise to the compensation, or at such other time as provided in regulations. A special 30-day election period applies for newly eligible participants. The Ways and Means Committee report states that it is expected that Treasury regulations will provide that, in appropriate circumstances, an election to defer an incentive bonus earned over a period of several years may be made after the service period begins, as long as the election is made no later than 12 months before the earliest date on which the bonus is payable. Report also</p>	<p>Same, except does not contain report language like that in the Ways and Means Committee report regarding expected regulations on elections to defer multi-year incentive bonuses being made 12 months before payment, or the consideration of factors such as when the amount of the bonus payment is determinable.</p>

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	provides that Treasury may consider other factors, such as when the amount of the bonus payment is determinable, but that Treasury regulations may not permit any deferral election if the timing of the election would be inconsistent with the purposes of the provision.	
Restrictions on "Subsequent Elections"	Any subsequent election to delay the timing or change the form of payment generally must (1) not take effect until at least 12 months after the date of the election, (2) except in the case of elections relating to distributions on death, disability, or unforeseeable emergency, provide an additional deferral for a period of at least 5 years from the date such payment would otherwise have been made, and (3) if related to a payment at a specified time or pursuant to a fixed schedule, be made at least 12 months prior to the date of the first scheduled payment. No acceleration of payments (<u>e.g.</u> , from an annuity to a lump sum) is permitted, but Treasury may provide, through regulations, limited exceptions to the general rule in cases where accelerated distribution is required for reasons beyond the control of the participant. Treasury also is expected to issue guidance regarding to what extent elections to change a stream of payments are permissible.	Same, except only one subsequent election is permitted with respect to an amount deferred.
Restrictions on Investment Control	None.	Investment options must be comparable to those which may be elected under the qualified defined contribution plan of the employer with the fewest investment options. If there is no such qualified defined contribution plan, the investment options must satisfy such requirements as Treasury may prescribe, including requirements limiting the options to certain specified options. (The Finance Committee's report on the NESTEG pension reform bill provides that the Committee intends that the nonqualified plan investment options may be less favorable or more

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		limited than the qualified plan options, and that the Committee intends that open brokerage windows, hedge funds, and investments in which the employer guarantees a rate of return above what is commercially available, are prohibited.)
Effect on Domestic Rabbi Trusts	None.	None.
Effect on Offshore Rabbi Trusts	Assets sets aside (directly or indirectly) in an offshore trust for the purposes of paying nonqualified deferred compensation are treated as property transferred under IRC section 83 at the time set aside or transferred outside the U.S., whether or not the assets are available to satisfy claims of general creditors. Earnings on such assets are treated as additional transfers of property. Thus, participants would be immediately taxed on deferred amounts when no longer subject to a substantial risk of forfeiture. Interest at the underpayment rate plus one percent is imposed on the underpayments that would have occurred had the amounts been includible in income for the taxable year in which first deferred or, if later, the first taxable year in which such amounts are not subject to a substantial risk of forfeiture. Treasury is granted regulatory authority to provide exceptions for arrangements that will not result in the improper deferral of tax and where assets will not be effectively beyond the reach of creditors.	Same, except there also is a specific exception for assets located in a foreign jurisdiction if substantially all of the services to which the deferred compensation relates are performed in such foreign jurisdiction. Interest at the underpayment rate is imposed, and the amount required to be included in income is also subject to an additional ten percent tax.
Treatment of Financial Distress Triggers	In the case of compensation deferred under a nonqualified deferred compensation plan, a transfer of property occurs under IRC section 83 with respect to the deferred compensation if the plan provides that, upon a change in the employer's financial health, assets will be restricted to the payment of benefits. Earnings on such assets are treated as additional transfers of property.	Generally the same. Interest at the underpayment rate is imposed, and the amount required to be included in income is also subject to an additional ten percent tax.

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Restrictions on Deferral of Stock Option Gains/ Restricted Stock	None.	Gains attributable to stock options, vesting of restricted stock, employer securities, or any other property based on employer securities transferred to the taxpayer, could not be deferred by electing to instead receive deferred amounts. Taxpayers would be taxed immediately on the present value of the right to receive future payments obtained in exchange for the stock options, employer securities, or other property based on employer securities transferred to the taxpayer.
Treasury Regulatory Authority	Treasury is directed to issue regulations to carry out the purposes of these new rules, including regulations on the treatment of nonqualified defined benefit plans, changes in control of a corporation, and provisions for disregarding a substantial risk of forfeiture where necessary to carry out the purposes of the legislation.	Same. (The Finance Committee NESTEG pension reform bill – but not the JOBS Act – also repeals the longstanding limitation (sec. 132 of the Revenue Act of 1978) on the issuance of Treasury guidance on nonqualified deferred compensation, and directs Treasury to issue guidance on arrangements that improperly defer income, consistent with the other provisions of the legislation.)
Reporting Requirements	Deferred amounts are required to be reported to the IRS as part of an individual's Form W-2 for the year deferred (even if the amounts are not currently taxable).	Same.

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Withholding Changes	None.	Withholding is increased to the highest income tax rate (35 percent for 2003) on supplemental wage payments (<u>e.g.</u> , bonuses and commissions) to an employee to the extent that annual supplemental payments to the employee exceed \$1 million.
Effective Date	Amounts deferred after June 3, 2004. (The Ways and Means Committee report provides that amounts further deferred under a subsequent election with respect to amounts originally deferred before June 4, 2004, are subject to the amendments.) The amendments do not apply to amounts deferred after June 3, 2004, and before January 1, 2005, pursuant to an irrevocable election or binding arrangement made before June 4, 2004. The amendments apply to earnings on deferred amounts only to the extent that such deferred amounts are subject to the proposed amendments. Treasury is directed to issue guidance within 90 days of enactment providing a limited period of time during which participants in a nonqualified deferred compensation plan adopted before June 4, 2004, could terminate participation or cancel an outstanding deferral election with regard to amounts earned after June 3, 2004, provided that those amounts are includible in income as earned.	Amounts deferred after December 31, 2004. The withholding provision is effective for payments made after December 31, 2003, and the restriction on stock option/restricted stock deferrals is effective for exchanges after December 31, 2004. The amendments apply to earnings on deferred amounts only to the extent that such deferred amounts are subject to the proposed amendments. Treasury is directed to issue guidance within 90 days of enactment providing a limited period of time during which participants in a nonqualified deferred compensation plan adopted on or before December 31, 2004, could terminate participation or cancel an outstanding deferral election with regard to amounts earned after December 31, 2004, provided that those amounts are includible in income as earned.
JCT Revenue Estimate	Raises approximately \$800 million/10 years.	Raises approximately \$1 billion/10 years.