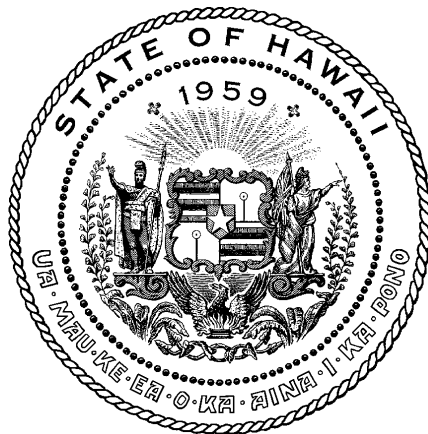


ENACTED BY THE STATE OF HAWAII

2005 Digest of Tax Measures

TWENTY-THIRD LEGISLATURE
REGULAR AND SPECIAL SESSIONS



Prepared by the State of Hawaii
Department of Taxation
December 31, 2005

NOTE: This Digest is issued solely as a guide and is not intended to be complete.

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Introduction

The following is a digest of bills passed by the 2005 Legislature and enacted into law. The Governor vetoed one substantive tax measure. The digest includes only those measures that affect Hawaii's tax laws and is provided for your information. It is issued solely as a guide and is not intended to be either authoritative or complete. Copies of the bills passed by the Legislature may be obtained from the Senate and House printshops. Bills and Acts are also accessible via the Internet on the State Capitol website at <http://www.capitol.hawaii.gov>, or on the Department of Taxation's website at <http://www.hawaii.gov/tax/>.

KEY TO ABBREVIATIONS

| | | |
|----------|---|---|
| SB | = | Senate Bill |
| SD | = | Senate Draft |
| HB | = | House Bill |
| HD | = | House Draft |
| CD | = | Conference Draft |
| SCR | = | Senate Concurrent Resolution |
| HCR | = | House Concurrent Resolution |
| SSCR | = | Senate Standing Committee Report |
| HSCR | = | House Standing Committee Report |
| CCR | = | Conference Committee Report |
| SECT AFF | = | Section(s) of the Hawaii Revised Statutes Affected by the Bill's Provisions |
| HRS | = | Hawaii Revised Statutes |
| HAR | = | Hawaii Administrative Rules |
| SLH | = | Session Laws of Hawaii |

ADMINISTRATIVE TAX MEASURES

ACT 167

SB 460, HD1

RELATING TO TAX REFUNDS

SSCR 664, HSCR 1546

SECT AFF: 232-14.5

Restates that taxpayers may appeal a denial of a tax refund claim by filing a written notice of appeal to the board of review or to the tax appeal court within 30 days after notice of the denial of the claim. Allows taxpayers to file an appeal of a refund claim when the Department of Taxation fails to act on the claim within 180 days after the claim was filed.

EFFECTIVE: June 28, 2005, and applies to tax refund claims filed after June 30, 2005.

Act 3, Special Session

HB 1224, SD1, CD1

RELATING TO TAXATION

HSCR 778, SSCR 1477, CCR 149

SECT AFF: 231-3.6, 255D-3, 255D-4

Establishes requirements, procedures, standards, and guidelines for compliance with the Streamlined Sales and Use Tax Agreement project. Allows contractors contracted by the Legislative Auditor to support the project to inspect tax returns and other information for the purposes of conforming the State's general excise and use taxes to the Model Agreement and Act. Appropriates \$50,000 to be expended by the Legislative Auditor.

EFFECTIVE: July 12, 2005; provided that the appropriation section takes effect on July 1, 2005.

ACT 9, Special Session

SB 1685, SD2, HD1, CD1

RELATING TO TAX

SSCR 162, SSCR 833, HSCR 1552, CCR 14

SECT AFF: 46-1.8, 231-18, 235-117, 237D-13

Authorizes the Department of Taxation (Department) to share tax return information with the county directors of finance and their staffs for tax purposes. Also, authorizes the county directors of finance to share confidential tax return information with the Department notwithstanding any other laws (or ordinances) to the contrary.

EFFECTIVE: July 12, 2005.

GENERAL EXCISE / USE / PSC TAX MEASURES

ACT 146

SB 1453, SD2, HD1, CD1

RELATING TO PUBLIC SERVICE COMPANY TAX

SSCR 208, SSCR 776, HSCR 1053, HSCR 1193, HSCR 1503, CCR 21

SECT AFF: 239-2

Imposes the public service company tax on the gross income of a private sewer company or facility. Applies to gross income derived from operation as a private sewer company or private sewer facility that accrued beginning July 1, 2005.

EFFECTIVE: July 1, 2005.

ACT 196

SB 179, SD3, HD2, CD1

RELATING TO HOUSING

SSCR 20, SSCR 545, SSCR 764, HSCR 1214, HSCR 1632, CCR 181

SECT AFF: 46-14.5, 201G-116, 201G-432, 201G-435, 201G-436, 247-3, 201G-44, 201G-461, 201G-118, 201G-123, 201G-411, 201G-3, 201G-7, 201G-8, 201G-14, 201G-15, 201G-431, 201G-433, 201G-434, CHAPTER 201H (22 SECTIONS)

Provides incentives for private developers to build affordable housing projects by establishing a general excise tax exemption for developers of housing projects certified by the Housing and Community Development Corporation (HCDCH) when:

- (1) At least 50 percent of the available units are for households with incomes at or below 80 percent of the median family income; and
- (2) At least 20 percent are for households with incomes at or below 60 percent of the median family income.

Also, authorizes the HCDCH to establish and collect a service fee in connection with the certification process.

EFFECTIVE: July 1, 2005.

ACT 247

HB 1309, HD2, SD2, CD1

RELATING TO TAXATION

HSCR 162, HSCR 953, SSCR 1096, SSCR 1569, CCR 186

SECT AFF: 46-16.8, 237-8.6, 238-2.6, 248-2.6, CHAPTER 51D

Allows counties the option of adding a surcharge of no more than 0.5 percent to the State's 4 percent general excise tax (GET) to be levied not earlier than January 2007 to fund public transportation systems in the respective counties. To levy a surcharge, a county must adopt an ordinance by December 31, 2005. The surcharge shall not apply to transactions: (1) subject to the 0.5 percent state GET rate; (2) subject to the 0.15% GET rate (i.e., insurance commissions); and (3) amounts, persons, gross income, or gross proceeds exempt from the state GET.

The Department of Taxation is required to levy, assess, collect, and administer the county surcharge for the counties.

EFFECTIVE: July 12, 2005 (without Governor's signature); provided that the counties adopt an ordinance to levy the surcharge by December 31, 2005, and the surcharge is repealed on December 31, 2022.

INCOME TAX MEASURES

ACT 23

SB 842, SD1 <TAX-13>

RELATING TO WITHHOLDING OF TAX ON THE DISPOSITION OF REAL PROPERTY BY NONRESIDENT PERSONS

SSCR 662, HSCR 1365

SECT AFF: 235-68

Closes a loophole by clarifying that where the single member Limited Liability Company (LLC) has not elected to be taxed as a corporation, the Hawaii Real Property Tax Act (HARPTA) withholding tax provisions are to be applied without regard to the existence of the LLC, and instead the residency of the single-member would be considered to determine whether HARPTA applies to the transaction.

Nothing in this Act shall be construed to create any inference with respect to the property tax treatment of single member LLCs for taxable years prior to the taxable year beginning on January 1, 2005.

EFFECTIVE: April 22, 2005, and applies to taxable years beginning after December 31, 2004.

ACT 27
SB 840, SD1 <TAX-10>
RELATING TO INCOME TAX WITHHOLDING
SSCR 663, HSCR 1096, HSCR 1524
SECT AFF: 235-62

Clarifies the State withholding tax provisions enacted during the 2004 legislative session as Act 113, SLH 2004. Requires employers whose liability for taxes exceeds \$40,000 annually to remit the complete amount of the tax withheld on a semi-weekly schedule.

Act 27 conforms our state tax provisions to federal withholding provisions by defining "semi-weekly schedule" to mean:

- (1) On or before the following Wednesday if wages were paid on the immediately preceding Wednesday, Thursday, or Friday; or
- (2) On or before the following Friday if wages were paid on the immediately preceding Saturday, Sunday, Monday, or Tuesday.

Incorporates the federal three-day banking rule by providing that each employer shall have at least three banking days following the close of the semi-weekly period by which to remit the taxes withheld as provided in section 6302 of the Internal Revenue Code. Also, requires that all income tax withholding returns be filed with the Director of Taxation in the First Taxation District, rather than in the taxation district which the employer's principal place of business.

EFFECTIVE: April 25, 2005.

ACT 60
SB 834, SD2, HD1 <TAX-01>
RELATING TO CONFORMITY OF THE HAWAII INCOME TAX LAW TO
THE INTERNAL REVENUE CODE
SSCR 615, SSCR 914, HSCR 1550
SECT AFF: 235-2.3, 235-2.4, 235-2.45

Section 235-2.5(c), HRS, mandates that the Department of Taxation submit a bill to the Legislature, during each regular session, to conform to the changes in the Internal Revenue Code (IRC). The adoption of the amendments to the IRC and the provisions of Public Law 109-001 assure continued State conformity with the federal income tax law and minimize taxpayers' burdens in complying with Hawaii's income tax law.

Reviewed were the federal income tax law changes resulting from the following federal acts:

- (1) The Pension Funding Equity Act of 2004 (P. L. No. 108-218, April 10, 2004);

- (2) The Working Families Tax Relief Act of 2004 (P. L. No. 108-311; October 4, 2004);
- (3) The American Jobs Creation Act of 2004 (P. L. No. 108-357, October 22, 2004);
- (4) An Act to accelerate the income tax benefits for charitable cash contributions for the relief of victims of the Indian Ocean tsunami (P.L. No. 109-001, January 7, 2005); and
- (5) Sec. 201. Disclosure of tax information in terrorism and national security investigations (P.L. 107-134, January 23, 2002).

For more information on the federal laws that the State will conform to, please see Announcement 2005-12 and/or the Digest of Federal Laws starting on page 16 of this publication.

EFFECTIVE: May 19, 2005 and applies to taxable years beginning after December 31, 2004.

ACT 116

SB 116, SD2, HD2, CD1

RELATING TO NURSES

SSCR 422, SSCR 815, HSCR 1141, HSCR 1603

SECT AFF: CHAPTER 304E (5 SECTIONS)

Encourages nurses to enroll in masters and doctoral programs that will prepare them for academic careers in nursing by:

- (1) Establishing a nursing scholarship program; and
- (2) Exempting scholarship grants under the program from taxable income.

EFFECTIVE: July 1, 2005.

ACT 196

SB 179, SD3, HD2, CD1

RELATING TO HOUSING

SSCR 20, SSCR 545, SSCR 764, HSCR 1214, HSCR 1632, CCR 181

SECT AFF: 46-14.5, 201G-116, 201G-432, 201G-435, 201G-436, 247-3, 201G-44, 201G-461, 201G-118, 201G-123, 201G-411, 201G-3, 201G-7, 201G-8, 201G-14, 201G-15, 201G-431, 201G-433, 201G-434, CHAPTER 201H (22 SECTIONS)

Provides incentives for developers to build affordable housing projects by increasing the low-income housing tax credit from 30 to 50 percent of the applicable percentage of the qualified basis of each building located in Hawaii.

Also, improves administration of the low-income housing tax credit by creating the Hawaii Housing Finance and Development Administration and designating it as the state housing credit agency to administer the low-income housing tax credit.

EFFECTIVE: July 1, 2005.

MISCELLANEOUS TAX MEASURES

ACT 58

HB 631, HD1, SD2, CD1

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

HSCR 76, HSCR 874, SSCR 1116, SSR 1607, CCR 138

SECT AFF: 88-81.5, 88-23, 88-47, 88-59, 88-59.5, 88-74, 88-76, 88-80, 88-85, 88-94, 88-96, 88-97, 88-102, 88-124, 88-126, 88-251, 88-261, 88-282, 88-285, 88-311, 88-321, 88-322, 88-324, 88-332, 88-333, 88-335, 88-337, 88-341

Clarifies and corrects the Employees' Retirement System (ERS) statutes and conforms ERS statutes to current practices. Among other things, requires the ERS to comply with federal income tax limits on compensation in determining ordinary death benefits.

EFFECTIVE: July 1, 2005; provided that the federal limits on annual compensation for ordinary death benefits takes effect retroactively to July 1, 1996.

ACT 67
HB 390, HD1, SD2, CD1
RELATING TO RENTAL MOTOR VEHICLE SURCHARGE TAX
HSCR 433, HSCR 866, SSCR 1056, SSCR 1609
SECT AFF: 251-2

Permanently exempts lessors from the rental motor vehicle surcharge tax if:

- (1) The lessor rents the vehicle to replace a vehicle of the lessee that is being repaired; and
- (2) The repair order for the vehicle is retained by the lessor for four years for verification purposes.

EFFECTIVE: May 23, 2005

ACT 82
HB 785, HD1, SD1, CD1
RELATING TO MORTGAGE FORECLOSURES
HSCR 744, SSCR 1311, CCR 73
SECT AFF: 667-61, 667-62, 667-63, 667-64, 667-65

Authorizes nonjudicial foreclosure of timeshare interests under a power of sale if:

- (1) The mortgagee or the mortgagee's successor in interest gives notice of the intent to foreclose upon a mortgage; and
- (2) Copies of the notice are filed with the Director of Taxation and posted on the premises of the timeshare interest not less than 21 days before the day of the sale.

EFFECTIVE: January 1, 2006.

ACT 131
SB 682, SD2, HD3, CD1
RELATING TO TOBACCO
SSCR 172, SSCR 804, HSCR 1075, HSCR 1270, HSCR 1609, CCR 112
SECT AFF: 245-2, 245-2.5, 245-2.6, 245-2.7

Requires businesses engaged in the sale of cigarettes and other tobacco products at the retail level to obtain a retail tobacco permit from the Department of Taxation beginning December 1, 2006. Imposes a \$20 fee for the permit which will be valid for one year, from December 1 to November 30, and renewable annually.

Beginning March 1, 2007, it will be a criminal offense for any retailer to sell, possess, keep, acquire, distribute, or transport cigarettes and other tobacco products without a valid retail tobacco permit.

A retail permit holder is required to provide the Department of Taxation with any information deemed necessary to verify compliance with this new law. The permit holder is also required to keep complete and accurate records of their cigarette or tobacco product inventory. The Department of Taxation may suspend or after a hearing, revoke, or decline to renew any retail tobacco permit or tobacco license if the applicant or permittee has failed to comply with chapter 245 or any rule adopted under that chapter, or for good cause.

EFFECTIVE: June 16, 2005; provided that the Act is repealed on July 1, 2009 and reenacted in the same form prior to the reenactment of this Act.

ACT 152

HB 477, HD1, SD1, CD1

RELATING TO EXEMPTING ROTH INDIVIDUAL RETIREMENT

ACCOUNTS FROM ATTACHMENT OR SEIZURE

HSCR 250, SSCR 1174, SSCR 1417, CCR 72

SECTION AFF: HSCR 651-124

Protects Roth Individual retirement accounts from the claims of creditors in the same manner as regular individual retirement accounts.

EFFECTIVE: June 23, 2005.

ACT 156

HB 1308, HD1, SD2, CD1

RELATING TO LAND CONSERVATION

HSCR 473, HSCR 879, SSCR 1261, SSCR 1591, CCR 146

SECT AFF: 36-27, 174A-2, 174A-35, 173A-9, 173A-10, 247-2, 247-7,

Establishes a permanent funding for land conservation by:

- (1) Amending § 247-2, HRS, to impose the following rate schedule on all transfers or conveyances of realty or any interest therein:
 - ◆ 10 cents per \$100 for properties with a value of less than \$600,000;
 - ◆ 20 cents per \$100 for properties with a value of \$600,000, but less than \$1,000,000; and
 - ◆ 30 cents per \$100 for per \$100 for properties with a value of \$1,000,000 or more.

Further provided that if the conveyance involves the sale of a condominium or single-family residence for which the purchaser is ineligible for a county homeowner's exemption from real property tax, the following rate schedule applies:

- ◆ 15 cents per \$100 for properties with a value of less than \$600,000;
- ◆ 25 cents per \$100 for properties with a value of \$600,000, but less than \$1,000,000; and
- ◆ 35 cents per \$100 for per \$100 for properties with a value of \$1,000,000 or more.

- (2) Requiring that revenues collected from the conveyance tax be allocated as follows: 10 percent to the Land Conservation Fund; 30 percent to the Rental Housing Trust Fund; 25 percent to the Natural Area Reserve Fund; and 35 percent to the General Fund.

EFFECTIVE: July 1, 2005. The new conveyance tax rates will apply to any conveyance of real property executed on or after July 1, 2005.

ACT 183

HB 1640, HD3, SD2, CD1

RELATING TO IMPORTANT AGRICULTURAL LANDS

HSCR 194, HSCR 531, HSCR 968, SSCR 1281, SSCR 1592, CCR 175

SECT AFF: 205-3.1, 205-4, 205-6, 205-17, 205-41, 205-42, 205-43, 205-44, 205-45, 205-46, 205-47, 205-48, 205-49, 205-50, 205-51, 205-52

Establishes State and county policies and procedures for identifying important agricultural lands. Requires the Department of Agriculture, with the assistance of the Department of Taxation, to conduct a study and develop proposals for agricultural incentives.

EFFECTIVE: July 1, 2005.

ACT 211

SB 1127, SD1

RELATING TO THE PUBLIC PROCUREMENT CODE

SSCR 407, SSCR 905, HSCR 1205, HSCR 1789

SECT AFF: 103D-310

Eliminates the requirement that small purchase contracts awarded (less than \$25,000) by the State must obtain tax clearances, certificates of good standings, and certificates of compliance.

EFFECTIVE: July 8, 2005.

ACT 235

SB 1729, SD2, HD2, CD1

RELATING TO TOURISM

SSCR 459, SSCR 997, HSCR 1102, HSCR 1608, CCR 177

SECT AFF: 184-3.4, 198D-2, 201B-2, 201B-3, 201B-8, 201B-11, 237D-6.5, 237D-5.5

Improves tourism-related activities and provides a dedicated source of funding for the Hawaii Tourism Authority by:

- (1) Increasing the transient accommodations tax allocation to the Tourism Special Fund to 34.2 percent;
- (2) Requiring excess TAT revenues to be deposited into the general fund;
- (3) Repealing the TAT Trust Fund; and
- (4) Revising the allocation of the TAT revenues for the State Parks Special Fund and the Special Land and Development Fund.

EFFECTIVE: July 1, 2005; provided that the TAT increase to the Tourism Special Fund and the repeal of the TAT Trust Fund takes effect on July 1, 2007.

VETOED MEASURES

VETOED (JULY 11, 2005)

HB 1554, HD2, SD2, CD1

RELATING TO LEASEHOLD CONVERSION

HSCR 169, HSCR 415, HSCR 791, SSCR 1105, SSCR 1618, CCR 147

SECT AFF: 235-7

Allows a fee owner of residential leasehold property to exclude, from the fee owner's taxable income, up to 50 percent of the proceeds the fee owner receives from the sale, provided that the exclusion does not exceed \$75,000 in the aggregate for all taxpayers in the State in any tax year. In effect, this amounts to a tax credit for only a few people who sell their leased fee interest.

TABLE SHOWING EFFECT OF ACTS

Twenty-Third Legislature - 2005 Regular and Special Sessions

| | |
|-------------------|--|
| KEY: Am = Amended | R = Repealed |
| N = New | ___ = Chapter or section number to be assigned in HRS Supplement |

| SECTIONS OF HRS AFFECTED | | | |
|--------------------------|--------|-------------|------------------------|
| SECTION NO. | EFFECT | ACT NO. | BILL NO. |
| 36-27 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 46-1.8 | N | ACT 9, L Sp | SB 1685, SD2, HD1, CD1 |
| 46-14.5 | N | ACT 196 | SB 179, SD3, HD2, CD1 |
| 46-16.8 | N | ACT 247 | HB 1309, HD2, SD2, CD1 |
| 88-81.5 | N | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-23 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-47 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-59 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-59.5 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-74 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-76 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-80 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-85 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-94 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-96 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-97 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-102 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-124 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-126 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-251 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-261 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-282 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-285 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-311 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-321 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-322 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-324 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-332 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-333 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-335 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-337 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 88-341 | Am | ACT 58 | HB 631, HD1, SD2, CD1 |
| 103D-310 | Am | ACT 211 | SB 1127, SD1 |
| 173A-2 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |

TABLE SHOWING EFFECT OF ACTS
 TWENTY-THIRD LEGISLATURE - 2005 REGULAR AND SPECIAL SESSIONS

| SECTIONS OF HRS AFFECTED | | | |
|---------------------------------|---------------|----------------|------------------------|
| SECTION NO. | EFFECT | ACT NO. | BILL NO. |
| 173A-5 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 173A-9 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 173A-10 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 184-3.4 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 198D-2 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 201B-2 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 201B-3 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 201B-8 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 201B-11 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 201G-3 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-7 | R | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-8 | R | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-14 | R/Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-15 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-44 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-116 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-118 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-123 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-411 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-431 | R | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-432 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-433 | R | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-434 | R | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-435 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-436 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 201G-461 | Am | ACT 196 | SB 179, SD3, HD2, CD1 |
| 205-3.1 | Am | ACT 183 | HB 1640, HD3, SD2, CD1 |
| 205-4 | Am | ACT 183 | HB 1640, HD3, SD2, CD1 |
| 205-6 | Am | ACT 183 | HB 1640, HD3, SD2, CD1 |
| 205-17 | Am | ACT 183 | HB 1640, HD3, SD2, CD1 |
| 231-3.6 | N | ACT 3, L Sp | HB 1224, SD1, CD1 |
| 231-18 | Am | ACT 9, L Sp | SB 1685, SD2, HD1, CD1 |
| 232-14.5 | N | ACT 167 | SB 460, HD1 |
| 235-2.3 | Am | ACT 60 | SB 834, SD2, HD1 |
| 235-2.4 | Am | ACT 60 | SB 834, SD2, HD1 |
| 235-2.45 | Am | ACT 60 | SB 834, SD2, HD1 |
| 235-7 | Am | Veto | HB 1554, HD2, SD2, CD1 |
| 235-62 | Am | ACT 27 | SB 840, SD1 |
| 235-68 | Am | ACT 23 | SB 842, SD1 |
| 235-117 | Am | ACT 9, L Sp | SB 1685, SD2, HD1, CD1 |
| 237-8.6 | N | ACT 247 | HB 1309, HD2, SD2, CD1 |
| 237D-5.5 | R | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 237D-6.5 | Am | ACT 235 | SB 1729, SD2, HD2, CD1 |
| 237D-13 | Am | ACT 9, L Sp | SB 1685, SD2, HD1, CD1 |

TABLE SHOWING EFFECT OF ACTS
 TWENTY-THIRD LEGISLATURE - 2005 REGULAR AND SPECIAL SESSIONS

| SECTIONS OF HRS AFFECTED | | | |
|--|---------------|----------------|------------------------|
| SECTION NO. | EFFECT | ACT NO. | BILL NO. |
| 238-2.6 | N | ACT 247 | HB 1309, HD2, SD2, CD1 |
| 239-2 | Am | ACT 146 | SB 1453, SD2, HD1, CD1 |
| 245-2 | Am | ACT 131 | SB 682, SD2, HD3, CD1 |
| 245-2.5 | N | ACT 131 | SB 682, SD2, HD3, CD1 |
| 245-2.6 | N | ACT 131 | SB 682, SD2, HD3, CD1 |
| 245-2.7 | N | ACT 131 | SB 682, SD2, HD3, CD1 |
| 247-2 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 247-3 | Am | ACT 196 | SB 179, SD3, HD2, CD |
| 247-7 | Am | ACT 156 | HB 1308, HD1, SD2, CD1 |
| 248-2.6 | N | ACT 247 | HB 1309, HD2, SD2, CD1 |
| 251-2 | Am | ACT 67 | HB 390, HD1, SD2, CD1 |
| 255D-3 | Am | ACT 3, L Sp | HB 1224, SD1, CD1 |
| 255D-4 | Am | ACT 3, L Sp | HB 1224, SD1, CD1 |
| 651-124 | Am | ACT 152 | HB 477, HD1, SD1, CD1 |
| 667-61 | N | ACT 82 | HB 785, HD1, SD1, CD1 |
| 667-62 | N | ACT 82 | HB 785, HD1, SD1, CD1 |
| 667-63 | N | ACT 82 | HB 785, HD1, SD1, CD1 |
| 667-64 | N | ACT 82 | HB 785, HD1, SD1, CD1 |
| 667-65 | N | ACT 82 | HB 785, HD1, SD1, CD1 |
| CHAPTERS AFFECTED | | | |
| CHAPTER NO. | EFFECT | ACT NO. | BILL NO. |
| 51D | R | ACT 247 | HB 1309, HD2, SD2, CD1 |
| 205 (12 sections) Important Agricultural Lands | N | ACT 183 | HB 1640, HD3, SD2, CD1 |
| NEW CHAPTERS | | | |
| CHAPTER SUBJECT | EFFECT | ACT NO. | BILL NO. |
| 201H (22 sections) Hawaii Housing Finance and Development Administration | N | ACT 196 | SB 179, SD3, HD2, CD |
| 304E (5 sections) Nursing Scholars Program | N | ACT 116 | SB 116, SD2, HD2, CD1 |

Digest of Working Families Tax Relief Act of 2004

(P. L. No. 108-311; October 4, 2004)

Note: Only amendments or additions to Internal Revenue Code Sections contained in subtitle A, chapter 1, and certain 6000 series sections of the Internal Revenue Code of 1986, as amended, are applicable for this Digest.

CODE SECTION DESCRIPTION OF PROVISION

The following provisions are operative for Hawaii income tax purposes.

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|---------------------------|---|
| § 2(a)(1)(B)(i) | Definition of surviving spouse. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| §§ 2(b)(1)(A) and 2(b)(2) | Definition of head of household. Incorporates the uniform definition of child (as defined in IRC § 152(c) determined without regard to IRC § 152(e)). Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §202. |
| § 41(h)(1)(B) | Research credit. Extends the research credit to December 31, 2005. Applicable to amounts paid or incurred after June 30, 2004. Act §301(a)(1). |
| § 42(i)(3)(D)(ii)(I) | Low-income housing credit. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 62(a)(2)(D) | Adjusted gross income defined: certain expenses of elementary and secondary teachers. Extends the deduction to 2004 and 2005. Applicable to expenses paid or incurred in taxable years beginning after December 31, 2003. Act §307. |
| § 105 | Amounts received under accident and health plans. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 125(e)(1)(D) | Cafeteria plans. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 129(c)(2) | Dependent care assistance programs. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 132(h)(2)(B) | Certain fringe benefits. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
|---------------------|--|
| § 152 | Definition of dependent. Incorporates uniform definition of child and redefined dependent provisions. Effective for taxable years beginning after December 31, 2004. Act §201. |
| § 153 | Cross references. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 170(e)(6)(G) | Charitable contributions: special rule for contributions of computer technology and equipment for educational purposes. Extends the special rule to contributions made in taxable years beginning before January 1, 2006. Applicable to contributions made in taxable years beginning after December 31, 2003. Act §307. |
| § 170(g) | Charitable contributions: amounts paid to maintain certain students as members of taxpayer's household. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 179A(b)(1)(B) | Deduction for clean-fuel vehicles and certain refueling property. Eliminates the phase-out for deduction for clean-fuel vehicle property for 2004 and 2005. Effective for property placed in service after December 31, 2003. Act §319. |
| § 198(h) | Expensing of environmental remediation costs. Extends the deduction to 2004 and 2005. Applicable to expenditures paid or incurred after December 31, 2003. Act §308. |
| § 213 | Medical, dental, etc., expenses. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 220(d)(2)(A) | Archer MSAs: qualified medical expenses. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 220(i) | Archer MSAs: limitation on number of taxpayers having Archer MSAs. Extends the cut-off year to calendar year 2005. Effective on January 1, 2004. Act §322(a). |
| § 220(i) | Archer MSAs: limitation on number of taxpayers having Archer MSAs. Makes conforming amendments in connection with the extension of the cut-off year to calendar year 2005. Effective on January 1, 2004. Act §322(b). |
| § 221(d)(4) | Interest on education loans. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 529(e)(2)(B) | Qualified tuition programs. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207. |
| § 613A(c)(6)(H) | Limitation on percentage depletion in case of oil and gas wells: temporary suspension of taxable income limit with respect to marginal production. Extends such suspension to taxable years beginning before January 1, 2006. Effective for taxable years beginning after December 31, 2003. Act §314. |

CODE SECTION DESCRIPTION OF PROVISION

§ 691(c)(4) Recipients of income in respect of decedents: deduction for estate tax-coordination with capital gain provisions. Makes technical corrections to JGTRRA of 2003. Effective as if included in §302 of the JGTRRA of 2003. Act §402.

§§ 6103(i)(3)(C) and 6103(i)(7) Extends the period of time during which disclosures to law enforcement agencies or intelligence agencies may be made upon written request to Dec. 31, 2005. Section 201 of the Victims of Terrorism Tax Relief Act of 2001 has previously amended IRC section 6103 to authorize the disclosure of return information to the United States Justice Department or appropriate federal or state law enforcement agency for purposes of (a) investigating terrorist incidents, threats, or activities and (b) analyzing intelligence concerning investigating terrorist incidents, threats, or activities.

Return information includes the following information:

1. A taxpayer's identity, the nature, source or amount of income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, or tax payments;
2. Whether the taxpayer's return was, is being, or will be examined or subject to other investigation or processing;
3. Any other data, received by, recorded by, prepared by, furnished to, or collected by the Department of Taxation with respect to a return or with respect to the determination of the existence, or possible existence, of liability (or the amount thereof) of any person for any tax, penalty, interest, fine, forfeiture, or other imposition, or offense; and
4. The term "return information" does not include data in a form that cannot be associated with or otherwise identify, directly or indirectly, a particular taxpayer. "Taxpayer return information" means return information which is filed with, or furnished to, the Internal Revenue Service by or on behalf of the taxpayer to whom such return information relates.

If the Department of Taxation receives a written request meeting certain requirements, it may disclose return information (other than taxpayer return information) to officers and employees of any federal law enforcement agency who are personally and directly engaged in the response to, or investigation of, any terrorist incident, threat, or activity. However, no disclosure shall be made if disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

The written request must be made by the head of any federal law enforcement agency (or his delegate) involved in the response to or investigation of any terrorist incident, threat, or activity and set forth the specific reason or reasons why disclosure may be relevant to a terrorist incident, threat, or activity.

The head of any federal law enforcement agency may disclose return information obtained under such written request to officers and employees of any state or local law enforcement agency provided that such agency is part of a team with the federal law enforcement agency engaged in the response to, or investigation of, a terrorist incident, threat, or activity, and the information is disclosed only to officers and employees who are personally and directly engaged in that response or investigation. The information disclosed to officers and employees of law enforcement agencies shall be used only by them in that response or investigation. Officers and employees, and former officers and employees, of state and local law enforcement agencies shall not disclose any return or return information received under this rule, except as authorized by the IRC.

As a condition of receiving the above tax information, federal and state agencies must establish procedures satisfactory to the Department of Taxation to safeguard that information and return it or make it undisclosed when they are finished with it.

The Department of Taxation may disclose returns and taxpayer return information to the Attorney General to the extent necessary for, and solely for use in preparing, an application for ex parte court ordered disclosure initiated by the Department of Taxation.

Applicable to disclosures on or after October 4, 2004 and before January 1, 2006. Act §320(c)(1).

The following provisions are NOT operative for Hawaii income tax purposes.

- § 1(f)(8) Tax liability determination. Accelerates the marriage penalty phase-out for married taxpayers filing joint returns. The 15 percent regular income tax rate bracket is increased to twice the size of the 15 percent regular income tax rate bracket for single returns for taxable years beginning after December 31, 2003 and before January 1, 2008. Act §101(c).
- § 1(h) Tax liability determination: maximum capital gains rate. Makes technical corrections to JGTRRA of 2003. Effective as if included in §302 of the JGTRRA of 2003. Act §402.
- § 1(i)(1)(B) Tax liability determination. Accelerates the increase in the 10 percent rate bracket for married taxpayers filing joint returns. The initial bracket amount is increased from \$12,000 to \$14,000 for taxable years beginning after December 31, 2004 and before January 1, 2008. Act §101(d)(1).
- § 1(i)(1)(C) Tax liability determination. Accelerates the inflationary adjustments for married taxpayers filing joint returns and head of household filers by replacing the base year of 1992 with 2002 for taxable years beginning after December 31, 2003. Act §101(d)(2).
- § 21 Dependent care credit. Incorporates uniform definition of child and redefined dependent provisions and makes conforming amendments. Effective for taxable years beginning after December 31, 2004. Act §203.
- § 21(e) Dependent care credit. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207.
- § 24(a) Child tax credit. Increases to \$1,000 for 2005 through 2009. After 2010, the credit reverts to \$500 under the sunset provision of EGTRRA. Effective for taxable years beginning after December 31, 2003. Act § 101(a).
- § 24(c) Child tax credit. Incorporates uniform definition of child and makes conforming amendments. Effective for taxable years beginning after December 31, 2004. Act §204.
- § 24(d)(1) Child tax credit. Adds new provision to treat amounts excluded under IRC § 112 as earned income. Effective for taxable years beginning after December 31, 2003. Act §104(a).
- § 24(d)(1)(B)(i) Refundable portion of the child tax credit. Accelerates the increase in the refundable portion from 10 percent to 15 percent of the taxpayer's taxable earned income. Effective for taxable years beginning after December 31, 2003. Act §102.

- § 25B(c)(2)(B) Credit for elective deferrals and IRA contributions by certain individuals. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207.
- § 26(a) Allowance of nonrefundable personal credits against regular and minimum tax liability. Extends the allowance of such credits to 2004 and 2005. Adds provision that the limitations set forth in EGTRRA of 2001 shall not apply for 2004 and 2005. Effective for taxable years beginning after December 31, 2003. Act §312.
- § 26(b)(S) Allowance of nonrefundable personal credits against regular and minimum tax liability. Makes technical correction to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. Effective as if included in §1201 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. Act §401.
- § 30(b)(2) Credit for qualified electric vehicles. Eliminates the phase-out of credit for qualified electric vehicles for 2004 and 2005. Applicable to property placed in service after December 31, 2003. Act §318.
- § 32(c) Earned income credit. Incorporates uniform definition of child and makes conforming amendments. Effective for taxable years beginning after December 31, 2004. Act §205.
- §32(c)(2)(B) Earned income credit. Adds new provision to treat amounts excluded under IRC § 112 as earned income. Effective for taxable years beginning after October 4, 2004 and beginning before January 1, 2006. §104(b).
- § 35(g)(3) Credit for health insurance costs of eligible individuals. Makes technical correction to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. Effective as if included in §1201 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. Act §401. Act §401.
- § 45(c)(3) Credit for electricity produced from certain renewable resources. Extends the allowance of the credit for facilities placed in service before January 1, 2006. Effective for taxable years beginning after December 31, 2003. Act §313.
- § 45A(f) Indian employment credit. Extends the credit to taxable years beginning before January 1, 2006. Effective for taxable years beginning after December 31, 2004. Act §315.
- § 45C(b)(1)(D) Credit for clinical testing expenses for certain drugs for rare diseases or conditions. Extends the credit to December 31, 2005. Applicable to amounts paid or incurred after June 30, 2004. Act §301(a)(2).
- § 51(c)(4) Work opportunity tax credit. Extends the credit for wages paid or incurred on or before December 31, 2005. Applicable to individuals beginning work for the employer after December 31, 2003. Act §303.
- § 51(i) Work opportunity tax credit. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207.
- § 51A(f) Welfare to work tax credit. Extends the credit for wages paid or incurred on or before December 31, 2005. Applicable to individuals beginning work for the employer after December 31, 2003. Act §303.
- § 55(d)(1) Alternative minimum tax exemption. Expands the increased AMT exemption amount for married taxpayers filing joint returns and surviving spouses to taxable years beginning in 2005. Effective for taxable years beginning after December 31, 2004. Act §103.

- § 56 Alternative minimum tax: net operating loss deduction. Makes technical corrections to JCWAA of 2002. Effective as if included in the JCWAA of 2002. Act §403.
- § 63(c) Standard deduction. Increases the basic standard deduction amount for married taxpayers filing joint returns to twice the basic standard amount for single returns effective for 2005 through 2008. Makes conforming amendments to adjustments for inflation and applicable percentage table. Effective for taxable years beginning after December 31, 2003. Act §101(b).
- § 72(t) Additional tax on early distributions from qualified retirement plans. Makes technical and conforming amendments in connection with the incorporation of the uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §207.
- § 151(c) Personal exemption. Incorporates uniform definition of child. Effective for taxable years beginning after December 31, 2004. Act §206.
- § 168(j)(8) Accelerated depreciation for business property on Indian Reservation. Extends the accelerated depreciation to property placed in service before January 1, 2006. Effective for taxable years beginning after December 31, 2004. Act §316.
- § 168(k) Bonus depreciation Makes technical corrections to JCWAA of 2002. Effective as if included in the JCWAA of 2002. Act §403.
- § 172 Net operating loss carryback. Makes technical corrections to JCWAA of 2002. Effective as if included in the JCWAA of 2002. Act §403.
- § 904(h) Limitation on credit: taxes of foreign countries and of possessions of United States. Makes conforming amendments in connection with the extension of the allowance of personal credits against regular and minimum tax liability to 2004 and 2005. Effective for taxable years beginning after December 31, 2003. Act §312(b).
- § 1397E(e) Qualified zone academy bonds. Extends the credit to 2005. Applicable to obligations issued after December 31, 2003. Act §304.
- § 1400(f) Establishment of DC Zone. Extends the designation of the zone to period ending on December 31, 2005. Effective on January 1, 2004. Act §310(a).
- § 1400A(b) Tax-exempt economic development bonds. Extends the exemption to bonds issued on or before December 31, 2005. Applicable to bonds issued after October 4, 2004. Act §310(b).
- § 1400B Zero percent capital gains rate. Extends the exclusion of capital gains from the sale or exchange of any DC Zone asset held more than five years for which such asset was acquired before January 1, 2006. Makes conforming amendments. Effective on January 1, 2004. Act §310(c).
- § 1400C(i) First-time homebuyer credit for District of Columbia. Extends the allowance of the credit to property purchased before January 1, 2006. Effective on January 1, 2004. Act §310(d).
- § 1400F(d) Renewal community capital gain. Makes conforming amendment in connection with the extension of the exclusion of capital gains from the sale or exchange of any DC Zone asset held more than five years. Effective on January 1, 2004. Act §310(c).
- § 1400L(d)(2) Tax benefits for New York Liberty Zone. Extends the authority to issue Qualified New York Liberty Bond through December 31, 2009. Applicable to bond issued before January 1, 2010. Act §309(a).

§ 1400L(e) Tax benefits for New York Liberty Zone. Extends the allowance of an advance refund of certain bonds and clarifies the bonds eligible for advance refunds. Applicable to refunds made before January 1, 2006. Act §309(b) and §309(c).

Digest of the American Jobs Creation Act of 2004

(P. L. No. 108-357, October 22, 2004)

Note: Only amendments or additions to Internal Revenue Code Sections contained in subtitle A, chapter 1, and certain 6000 series sections of the Internal Revenue Code of 1986, as amended, are applicable for this Digest.

CODE SECTION DESCRIPTION OF PROVISION

The following provisions are operative for Hawaii income tax purposes.

- § 62 Adjusted gross income defined: deduction from gross income. Allows an above-the-line deduction, for any deductible attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with an action involving: a claim of unlawful discrimination; a claim of a violation of subchapter III of chapter 37 of title 31, United States Code, or a claim made under section 1862(b)(3)(A) of the Social Security Act. Applicable to fees and costs paid after October 22, 2004 with respect to any judgment or settlement occurring after October 22, 2004. Act §703.
- § 108(e)(8) Income from discharge of indebtedness: indebtedness satisfied by corporate stock or partnership interest. Requires partnerships to recognize the cancellation of indebtedness income upon the transfer of a capital or profits interest in the partnership to a creditor in satisfaction of a partnership debt. Applicable to cancellations of indebtedness occurring on or after October 22, 2004. Act §896.
- § 108(f) Income from discharge of indebtedness: student loans. Excludes payments to individuals under national health service corps loan repayment program and certain state loan repayment programs. Applicable to amounts received by an individual in taxable years beginning after December 31, 2003. Act §320.
- § 121 Exclusion of gain from sale of principal residence. Disallows the exclusion for gain on sale or exchange of a principal residence if the principal residence was acquired in a like-kind exchange in which any gain was not recognized within the prior five years. Applicable to sales or exchanges after October 22, 2004. Act §840.
- § 162(o) Trade or business expenses: treatment of certain expenses of rural mail carriers. Provides special rule for expenses exceeding reimbursements. If the reimbursements a rural letter carrier receives from the U.S. Postal Service fall short of the carrier's actual costs, the costs in excess of reimbursements qualify as a miscellaneous itemized deduction subject to the two-percent floor. Reimbursements in excess of their actual costs continue not to be required to be included in gross income. Effective for taxable years beginning after December 31, 2003. Act §318.
- § 163(l) Interest: disallowance of deduction on certain debt instruments of corporations. Expands disallowance of deduction for interest on convertible debt. Applicable to debt instruments issued after October 3, 2004. Act §845.

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
|---------------------------|---|
| § 163(m) | Interest: interest on unpaid taxes attributable to nondisclosed reportable transactions. Redesignates subsection (m) as subsection (n) and adds new IRC subsection (m) to disallow a deduction for interest on underpayments attributable to nondisclosed reportable transactions. Applicable to transactions in taxable years beginning after October 22, 2004. Act §838. |
| § 164(b) | Taxes: definitions and special rules – general sales tax. Allows for an election to take an itemized deduction for state and local general sales taxes instead of an itemized deduction for state and local income taxes. Effective for taxable years beginning after December 31, 2003 and before January 1, 2006. Act §501. |
| § 167(g) | Depreciation: depreciation under income forecast method - treatment of participation and residuals. Adds new subsection (7). Clarifies that, solely for purposes of computing the allowable deduction for property under the income forecast method of depreciation, participations and residuals may be included in the adjusted basis of the property beginning in the year such property is placed in service, but only if such participations and residuals relate to income to be derived from the property before the close of the tenth taxable year following the year the property is placed in service (as defined in Section 167(g)(1)(A)). Also clarifies that the income from the property to be taken into account under the income forecast method is the gross income from such property. Grants authority to Secretary to prescribe appropriate adjustments to the basis of property (and the look-back method) to reflect the treatment of participations and residuals. Applicable to property placed in service after October 22, 2004. Act §242. |
| §§ 167, 168, 197, and 470 | Reform of Tax Treatment of Certain Leasing Arrangements. Modifies the recovery period of certain property leased to a tax-exempt entity to the longer of the property's assigned class life or 125 percent of the lease term; alters the definition of lease term for all property leased to a tax-exempt entity so that the lease term includes all service contracts and other similar arrangements; expands the short-term lease exception for qualified technological equipment to exclude the renewal or extension lease options in determining the 5-year short-term lease exception; and establishes rules to limit deductions associated with leases to tax-exempt entities if the deductions exceed the taxpayer's gross income generated from such leases and if the leases do not satisfy specified criteria. Generally applicable to leases entered into after March 12, 2004. Act §§ 847 - 849. |
| § 168(e) | Accelerated cost recovery system: classification of property. Treats qualified leasehold improvements and restaurant property as 15-year recovery property and requires such qualified improvements and property to be depreciated using the straight-line method. Applicable to qualified leasehold improvements and restaurant property placed in service after October 22, 2004 and before January 1, 2006. Act §211. |
| § 168(e)(3)(C) | Accelerated cost recovery system: classification of property – classification of certain property – 7 year property. Treats qualified permanent motorsports racetrack complexes as 7-year recovery property. Applicable to qualified property placed in service after October 22, 2004 and before January 1, 2008. Act §704. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
|---------------------|--|
| § 170 | <p>Charitable, etc., contributions and gifts. Treatment of charitable contributions of patents and similar property; Increased reporting for noncash charitable contributions; and Donations of motor vehicles, boats, and airplanes valued at more than \$500.</p> <p>Tightens (a) the rules for deducting charitable contributions of (i) patents and similar property made after June 3, 2004, and (ii) motor vehicles, boats and airplanes made after December 31, 2004 and (b) the reporting rules for noncash charitable contributions for contributions made after June 3, 2004. Act §§ 882 – 884</p> |
| § 170(n) | <p>Charitable, etc., contributions and gifts. Redesignates subsection (n) as (o) and adds new subsection (n), expenses paid by certain whaling captains in support of native Alaskan subsistence whaling. Allows individuals to claim a deduction not exceeding \$10,000 per taxable year for certain expenses incurred in carrying out sanctioned whaling activities. The deduction is available only to an individual who is recognized by the Alaska Eskimo Whaling Commission as a whaling captain charged with the responsibility of maintaining and carrying out sanctioned whaling activities. The deduction is available for reasonable and necessary expenses paid by the taxpayer during the taxable year for: (1) the acquisition and maintenance of whaling boats, weapons, and gear used in sanctioned whaling activities; (2) the supplying of food for the crew and other provisions for carrying out such activities; and (3) the storage and distribution of the catch from such activities. For purposes of this provision, the term “sanctioned whaling activities” means subsistence bowhead whale hunting activities conducted pursuant to the management plan of the Alaska Eskimo Whaling Commission. Applicable to contributions made after December 31, 2004. Act §335.</p> |
| § 194 | <p>Treatment of reforestation expenditures: treatment as expenses and definitions and special rule.</p> <ol style="list-style-type: none">1. Allows up to \$10,000 of qualified reforestation expenditures to be deducted in the year paid or incurred (i.e., expensed) and allows qualified reforestation expenditures above \$10,000 to be amortized over 84 months;2. Disallows a deduction under any other provision (e.g. provision other than IRC section 194) with respect to any expenditure for which a deduction is allowed or allowable under IRC section 194;3. Disallows the benefit of the aforementioned deduction to trusts and estates (see following exception for estates); and4. Allows estates to amortize qualified reforestation expenditures in the same manner as in the case of an individual. <p>Applicable to expenditures paid or incurred after October 22, 2004. Act §322.</p> |
| § 195(b) | <p>Start-up expenditures: election to amortize - in general. Allows for an election to deduct up to \$5,000 of start-up expenditures in the taxable year in which the trade or business begins. The amount of start-up expenditures, for which the election to deduct up to \$5,000 is made, must be reduced by the amount of start-up expenditures exceeding \$50,000 (but not below zero) in the taxable year in which the trade or business begins. The amount that is not deductible must be amortized over a 180-month period beginning with the month in which the active trade or business begins. Applicable to amounts paid or incurred after October 22, 2004. Act §902(a).</p> |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
|---------------------------|--|
| §§ 167, 168, 197, and 470 | Reform of Tax Treatment of Certain Leasing Arrangements. Modifies the recovery period of certain property leased to a tax-exempt entity to the longer of the property's assigned class life or 125 percent of the lease term; alters the definition of lease term for all property leased to a tax-exempt entity so that the lease term includes all service contracts and other similar arrangements; expands the short-term lease exception for qualified technological equipment to exclude the renewal or extension lease options in determining the 5-year short-term lease exception; and establishes rules to limit deductions associated with leases to tax-exempt entities if the deductions exceed the taxpayer's gross income generated from such leases and if the leases do not satisfy specified criteria. Generally applicable to leases entered into after March 12, 2004. Act §§ 847 - 849. |
| § 197(e) | Extension of amortization of intangibles to sports franchises. Extends the 15-year recovery period for intangibles to franchises that engage in professional sports and any intangible asset acquired in connection with the acquisition of such franchise including player contracts. Applicable to property acquired after October 22, 2004. Act §866. |
| § 248(a) | Organizational expenditures: election to amortize. Allows for an election to deduct up to \$5,000 of organizational expenditures in the taxable year in which the trade or business begins. The amount of organizational expenditures, for which the election to deduct up to \$5,000 is made, must be reduced by the amount of organizational expenditures exceeding \$50,000 (but not below zero) in the taxable year in which the trade or business begins. The amount that is not deductible must be amortized over a 180-month period beginning with the month in which the active trade or business begins. Applicable to amounts paid or incurred after October 22, 2004. Act §902(b). |
| § 274(e)(2) | Disallowance of certain entertainment, etc., expenses: specific exceptions to application of subsection (a) – expenses treated as compensation. Limits the deduction for entertainment expenses involving specified individuals. Allows deduction for entertainment expenses for goods, services or facilities only to the extent of the amount of expenses are treated as compensation of specified individuals. Specified individuals include officers, directors, and 10 percent or greater owners of private and publicly held companies. Applicable to expenses incurred after October 22, 2004. Act §907. |
| § 334(b)(1) | Basis of property received in liquidations: liquidation of subsidiary – general rule. Limits transfers or importations of built-in-losses. Applicable to transactions and liquidations after October 22, 2004. Act §836(b). |
| § 338(h)(13) | Certain stock purchases treated as asset acquisitions: definitions and special rules – tax on deemed sale not taken into account for estimated tax purposes. Clarifies rules for payment of estimated tax for certain deemed asset sales with respect to qualified stock purchase for which an election is made under IRC section 338(h) (10). Applicable to transactions after October 22, 2004. Act §839. |
| § 351 | Clarification of definition of nonqualified preferred stock. Clarifies definition of qualified preferred stock for purposes of non-recognition of gain or loss on contributions of property in exchange for stock. This clarification is made to prevent taxpayers from characterizing an instrument as a qualifying preferred stock by including illusory participation rights or other terms. Applicable to transactions after May 14, 2003. Act §899. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 361(b)(3) | Nonrecognition of gain or loss to corporations; treatment of distributions: exchanges not solely in kind - treatment of distributions. Limits the amount of money and property that a distributing corporation can distribute to its creditors without gain recognition to the amount of the basis of the assets contributed to a controlled corporation in a divisive reorganization. Applicable to transfers of money or other property, or liabilities assumed, in connection with a reorganization occurring on or after October 22, 2004. Act §898. |
| § 362(e) | Basis to corporations: limitations on built-in-losses. Adds new subsection (e) to limit transfers or importations of built-in-losses. Applicable to transactions and liquidations after October 22, 2004. Act §836(a). |
| § 409A | Inclusion in gross income of deferred compensation under nonqualified deferred compensation plans. Provides specific rules as to whether deferral of income inclusion will be permitted. Under these new statutory rules, arrangements that allow participants inappropriate levels of control or access to deferred amounts will not result in deferral of income inclusion. Treats all amounts deferred under a non-qualified deferred compensation plan as gross income if such deferred amounts are not subject to a substantial risk of forfeiture (e.g., if the person's rights to such compensation are conditioned upon the performance of substantial services by any individual). Applicable to amounts deferred after December 31, 2004. Act §885. |
| § 421 | General rules: certain sales to comply with conflict-of-interest requirements. Treats as a qualifying disposition for purposes of deferral of gain and capital gain treatment, the sale of shares of stock in order to comply with federal conflict of interest requirements. Applicable to sales after October 22, 2004. Act §905. |
| §§ 421(b) and 423(c) | General rules: effect on disqualifying disposition and Employee stock purchase plan: special rules where option price is between 85 percent and 100 percent of value of stock. Adds provisions that income tax withholding is not required on a disqualifying disposition, nor when compensation is recognized in connection with an employee stock purchase plan discount. Applicable to stock acquired pursuant to options exercised after October 22, 2004. Act §§ 251(b) and (c). |
| § 451(e) | General rule for taxable year of inclusion: special rule for proceeds from livestock sold on account of drought, flood, or other weather-related conditions. Recognizes the extension of replacement period of involuntarily converted livestock (as provided by IRC section 1033(e)) for purposes of the special rule for livestock sold on account of weather-related conditions. Applicable to any taxable year with respect to which the due date (without regard to extensions) for the return is after December 31, 2002. Act §311(c). |
| § 453(f)(4)(B) | Installment method: definitions and special rules – purchaser evidences of indebtedness payable on demand or readily tradable. Denies installment sale treatment with respect to all sales in which the taxpayer receives indebtedness that is readily tradable. Applicable to sales occurring on or after October 22, 2004. Act §897. |
| §469 | Passive activity loss and credits limited. Net Income From Publicly Traded Partnerships (PTPs) Treated as Qualifying Income of Regulated Investment Companies (RICs). Provides that the special rule for publicly traded partnerships under the passive loss rules (requiring separate treatment) applies to a RIC holding an interest in a publicly traded partnership, with respect to items attributable to the interest in the publicly traded partnership. Effective for taxable years beginning after October 22, 2004. Act § 331. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| §§ 167, 168, 197, and 470 | Reform of Tax Treatment of Certain Leasing Arrangements. Modifies the recovery period of certain property leased to a tax-exempt entity to the longer of the property's assigned class life or 125 percent of the lease term; alters the definition of lease term for all property leased to a tax-exempt entity so that the lease term includes all service contracts and other similar arrangements; expands the short-term lease exception for qualified technological equipment to exclude the renewal or extension lease options in determining the 5-year short-term lease exception; and establishes rules to limit deductions associated with leases to tax-exempt entities if the deductions exceed the taxpayer's gross income generated from such leases and if the leases do not satisfy specified criteria. Generally applicable to leases entered into after March 12, 2004. Act §§ 847 - 849. |
| § 512(b) | Unrelated business taxable income: modifications. Adds new subsection (18), treatment of gain or loss on sale or exchange of certain brownfield sites. Excludes gain or loss on the sale, exchange, or other disposition of certain brownfield sites from unrelated business taxable income notwithstanding the rule that property held for sale to customers in the ordinary course of a trade or business is included in UBTI. Applicable to gain or loss on disposition of property acquired after December 31, 2004, but before January 1, 2010. Act §702(a). |
| § 512(e)(1) | Unrelated business taxable income: Special rules applicable to S-Corporations. Makes conforming amendment – expansion of bank S corporation eligible shareholders to include IRAs. Effective on October 22, 2004. Act §233(d). |
| § 514(b)(1) | Unrelated debt-financed income: definition of debt-financed property – in general. Adds new subparagraph (E) in connection with the new section 512(b)(18) relating to treatment of gain or loss on sale or exchange of certain brownfield sites. Applicable to gain or loss on disposition of property acquired after December 31, 2004, but before January 1, 2010. Act §702. |
| § 514(c)(6) | Unrelated debt-financed income: acquisition indebtedness - certain federal financing. Modifies the debt-financed property provisions by excluding from the definition of acquisition indebtedness any indebtedness incurred by a small business investment company licensed under the Small Business Investment Act of 1958 that is evidenced by a debenture (1) issued by such company under Section 303(a) of said Act, and (2) held or guaranteed by the Small Business Administration. The exclusion shall not apply during any period that any exempt organization (other than a governmental unit) owns more than 25 percent of the capital or profits interest in the small business investment company, or exempt organizations (including governmental units other than any agency or instrumentality of the United States) own, in the aggregate, 50 percent or more of the capital or profits interest in such company. Applicable to indebtedness incurred after October 22, 2004 by a small business investment company licensed after October 22, 2004. Act §247. |
| § 631(b) | Gain or loss in the case of timber, coal, or domestic iron ore: disposal of timber with a retained economic interest. Provides that outright sales of timber by a landowner will qualify for capital gains treatment in the same manner as sales with a retained interest. Applicable to sales after December 31, 2004. Act § 315. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| §§ 704(c), 734, 743, and 754 | Treatment of contributed property with built-in-loss. Restricts partnership allocations and elections in connection with built-in-loss properties and partnership basis adjustments. Results in (i) built-in-losses taken into account only by the contributing partner; (ii) allocations to non-contributing partners by the partnership on the assumption that the basis of the contributed property is its fair market value at the time of contribution; (iii) the requirement that the partnership shall make basis adjustments under IRC section 743 upon a transfer of partnership interest if the partnership has a substantial built-in-loss (over \$250,000); (iv) the requirement that property with a substantial built-in-loss shall be adjusted downward to its fair market value if the contributing partner's partnership interest is transferred or liquidated; and (v) the requirement that the partnership shall make basis adjustments under IRC section 743(b) with respect to any distribution of partnership property with respect to which there is a substantial basis reduction. Applicable to contributions, transfers, and distributions after October 22, 2004. Act §833. |
| § 709(b) | Treatment of organization and syndication fees. Allows for an election to deduct up to \$5,000 of organizational expenditures in the taxable year in which the partnership begins business. The amount of organizational expenditures, for which the election to deduct up to \$5,000 is made, must be reduced by the amount of organizational expenditures exceeding \$50,000 (but not below zero) in the taxable year in which the partnership begins business. The amount that is not deductible must be amortized over a 180-month period beginning with the month in which the partnership begins business. Should the partnership liquidate before the 180-month period, any remaining unamortized amount may be deducted to the extent allowable under section 165. Applicable to amounts paid or incurred after October 22, 2004. Act §902(b). |
| §§ 704(c), 734, 743, and 754 | Treatment of contributed property with built-in-loss. Restricts partnership allocations and elections in connection with built-in-loss properties and partnership basis adjustments. Results in (i) built-in-losses taken into account only by the contributing partner; (ii) allocations to non-contributing partners by the partnership on the assumption that the basis of the contributed property is its fair market value at the time of contribution; (iii) the requirement that the partnership shall make basis adjustments under IRC section 743 upon a transfer of partnership interest if the partnership has a substantial built-in-loss (over \$250,000); (iv) the requirement that property with a substantial built-in-loss shall be adjusted downward to its fair market value if the contributing partner's partnership interest is transferred or liquidated; and (v) the requirement that the partnership shall make basis adjustments under IRC section 743(b) with respect to any distribution of partnership property with respect to which there is a substantial basis reduction. Applicable to contributions, transfers, and distributions after October 22, 2004. Act §833. |
| § 755(c) | No allocation of basis decrease to stock of corporate partner. Precludes partnerships from decreasing the basis of its corporate partner's stock or any person related to its corporate partner in applying the basis allocation rules to a distribution in liquidation of a partner's interest. Allocates any decrease in basis, that would have been allocated to the stock, to other partnership assets. Recognizes gain by the partnership, to the extent of any excess of the decrease in basis over the basis of other partnership assets. Applicable to distributions after October 22, 2004. Act §834. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 851 | <p>Definition of regulated investment company. Net Income From Publicly Traded Partnerships (PTPs) Treated as Qualifying Income of Regulated Investment Companies (RICs). Modifies the 90-percent test with respect to income of a RIC to include net income derived from an interest in a publicly traded partnership and provides that net income from an interest in a publicly traded partnership is used for purposes of both the numerator and denominator of the 90-percent test. Also modifies the look-through rule for partnership income of a RIC so that it applies only to income from a partnership other than a publicly traded partnership and provides that the limitation on ownership and the limitation on composition of assets that apply to other investments of a RIC also apply to RIC investments in publicly traded partnership interests. Effective for taxable years beginning after October 22, 2004. Act § 331.</p> |
| §§ 856, 857, and 860 | <p>Definition of real estate investment trust; Taxation of real estate investment trusts and their beneficiaries, and Deduction for deficiency dividend.</p> <p>Improvements Related to Real Estate Investment Trusts (REITs)</p> <ol style="list-style-type: none">1. Modifies the definition of "straight debt" for purposes of the limitation that a REIT may not hold more than 10 percent of the value of the outstanding securities of a single issuer.2. Eliminates the rule requiring a REIT to own a 20 percent equity interest in a partnership in order for debt to qualify as "straight debt" and replaces with new "look-through" rules determining a REIT partner's share of partnership securities, generally treating debt to the REIT as part of the REIT's partnership interest for this purpose, except in the case of otherwise qualifying debt of the partnership.3. Provides specific safe-harbor rules regarding the dates for testing whether 90 percent of a REIT property is rented to unrelated persons and whether the rents paid by related persons are substantially comparable to unrelated party rents.4. Eliminates the safe harbor allowing rents received by a REIT to be exempt from the 100 percent excise tax if the rents are for customary services performed by the taxable REIT subsidiary (TRS) or are from a TRS and are described in Section 512(b)(3).5. Adds a provision under which, if a REIT fails to satisfy one or more requirements for REIT qualification, other than the 95 percent and 75 percent gross income tests and other than the new rules provided for failures of the asset tests, the REIT may retain its REIT qualification if the failures are due to reasonable cause and not willful neglect, and if the REIT pays a penalty of \$50,000 for each such failure.6. Allows a REIT to avoid disqualification if (1) the failure was due to reasonable cause and not willful neglect, (2) the failure is corrected, and (3) except for certain failures not exceeding a specified de minimis amount, a penalty is paid.7. Allows a REIT to declare a deficiency dividend after the REIT has identified a failure to pay the relevant amount. <p>Generally, effective for taxable year beginning after October 22, 2004. Act § 243.</p> |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 857(b)(6)(D) | Taxation of real estate investments trusts and their beneficiaries: method of taxation of real estate investment trusts and holders of shares or certificates of beneficial interest - income from prohibited transactions. Redesignates subparagraph D and E as E and F. Adds new subparagraph D, certain sales not to constitute prohibited transaction safe harbor. If the six requirements (as provided in new subparagraph D) are met, a sale of a real estate asset by a REIT will not be a prohibited transaction. Effective for taxable years beginning after October 22, 2004. Act § 321. |
| § 1033(e) and § 1033(f) | Involuntary conversions: livestock sold on account of drought, flood, or other weather-related conditions and replacement of livestock with other farm property where there has been environmental contamination. Extends the applicable period for a taxpayer to replace livestock sold on account of drought, flood, or other weather-related conditions from two years to four years after the close of the first tax year in which any part of the gain on conversion is realized. The extension is only available if a taxpayer establishes that, under the taxpayer's usual business practices, the sale would not have occurred but for drought, flood, or weather-related conditions that resulted in the area being designated as eligible for federal assistance. Effective for any taxable year with respect to which the due date (without regard to extensions) for the return is after December 31, 2002. Act §311. |
| § 1056 | Basis limitation for player contracts transferred in connection with the sale of a franchise. Repeals this section as a conforming amendment to the extension of amortization of intangibles to sports franchises (which extends the 15-year recovery period for intangibles to franchises that engage in professional sports and any intangible asset acquired in connection with the acquisition of such franchise including player contracts). Applicable to property acquired after October 22, 2004. Act §866. |
| § 1245(a) | Gain from disposition of certain depreciable property. Removes subsection (a)(4) as a conforming amendment to the extension of amortization of intangibles to sports franchises (which extends the 15-year recovery period for intangibles to franchises that engage in professional sports and any intangible asset acquired in connection with the acquisition of such franchise including player contracts). Applicable to franchises acquired after October 22, 2004. Act §866. |
| § 1253 | Transfers of franchises, trademarks, and trade names. Removes subsection (e)t as a conforming amendment to the extension of amortization of intangibles to sports franchises (which extends the 15-year recovery period for intangibles to franchises that engage in professional sports and any intangible asset acquired in connection with the acquisition of such franchise including player contracts). Applicable to property acquired after October 22, 2004. Act §866. |
| § 1301 | Averaging of farm income. Extends the benefits of income averaging to fishermen. Effective for taxable years beginning after December 31, 2003. Act §314(b). |
| § 1361(b) | S-Corporation defined: small business corporation. Increases the maximum number of shareholders from 75 to 100. Effective for taxable years beginning after December 31, 2004. Act §232. |
| § 1361(b) | S-Corporation defined: small business corporation-treatment of certain wholly owned subsidiaries. Authorizes the Secretary to provide guidance regarding information returns for qualified subchapter s subsidiary. Effective for taxable years beginning after December 31, 2004. Act §239. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 1361(c)(1) | S-Corporation defined: special rules for applying subsection (b) - members of family treated as one shareholder. Allows family members to elect to be treated as one shareholder for purposes of determining the number of shareholders of an S corporation. Effective for taxable years beginning after December 31, 2004. Act §231(a). |
| § 1361(c)(2) | S-Corporation defined: special rules for applying subsection (b) - certain trusts permitted as shareholders. Expands bank S corporation eligible shareholders to include IRAs. Effective on October 22, 2004. Act §233(a) and (b). |
| § 1361(d)(1) | S-Corporation defined: special rule for qualified subchapter S trust. Permits a beneficiary of a qualified Subchapter S trust (QSST) to deduct suspended losses under the at-risk and passive loss rules when the trust disposes of S stock by treating the disposition of the S corporation stock by the QSST as a disposition by the QSST beneficiary. Applicable to transfers made after December 31, 2004. Act §236. |
| § 1361(e)(2) | S-Corporation defined: electing small business trust defined - potential current beneficiary. Disregards unexercised powers of appointment in determining the potential current beneficiaries and increases the period during which the electing small business trust can dispose of stock after an ineligible shareholder becomes a potential current beneficiary from 60 days to one year. Effective for taxable years beginning after December 31, 2004. Act §234. |
| § 1362(d) | Election; revocation; termination: termination - where passive investment income exceeds 25 percent of gross receipts for 3 consecutive taxable years and corporation has accumulated earnings and profit. A bank (as defined in IRC section 581), a holding bank (as defined in section 2(a) of the Bank Holding Company Act of 1956), or a financial holding company (as defined in section 2(p) of the Bank Holding Company Act of 1956), earning interest and dividend income on assets required to be held by such bank or holding company may exclude such interest and dividend income for purposes of the S-Corporation passive investment income rules. Effective for taxable years beginning after December 31, 2004. Act §237. |
| § 1362(f) | Election; revocation; termination: inadvertent invalid elections or terminations. Provides additional relief from inadvertent invalid election or termination. Applicable to elections and terminations made after December 31, 2004. Act §231(b). |
| § 1362(f) | Election; revocation; termination: inadvertent invalid elections or terminations. Provides relief from inadvertent invalid qualified subchapter s subsidiary election and determinations. Applicable to elections made and terminations made after December 31, 2004. Act § 238. |
| § 1366(d)(2) | Pass-thru of items to shareholders: special rules for losses and deductions - indefinite carryover of disallowed losses and deductions. Provides an exception to the disallowance of suspended losses and deductions upon the transfer of S-Corporation stock from a shareholder to another with respect to stock transferred to a spouse or former spouse incident to divorce by treating the suspended losses or deductions as if incurred by the S-Corporation in the tax year following the stock transfer. Effective for taxable years beginning after December 31, 2004. Act §235. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 1388(a) | Definitions; special rules: patronage dividend. Provides that in computing the net earnings used to determine the amount of patronage dividends, a cooperative's net earnings are not reduced by amounts paid during the year as dividends on the organization's capital stock or other proprietary capital interests to the extent that the organization's articles of incorporation or bylaws or other contract with patrons provide that the dividends are in addition to amounts otherwise payable to patrons which result from business done with or for patrons during the tax year. Applicable to distributions made in taxable years beginning after October 22, 2004. Act §312. |
| § 1388(k) | Definitions; special rules: cooperative marketing includes value-added processing involving animals. Modifies the cooperative marketing rules to include value added processing involving animals by including, as marketing products of members or other producers, the feeding of products to cattle, hogs, fish, chickens, or other animals and the sale of the resulting animals or animal products. Effective for taxable years beginning after October 22, 2004. Act §316. |
| 1502 | NOTE: Section 235-92(2), HRS, references to IRC section 1502, and this amendment to IRC section 1502 is included in this digest solely for reference purposes. Regulations: Affirms the Treasury Department's authority to issue Treas. Regs. involving consolidated returns. Effective for taxable years beginning before, on, and after October 22, 2004. §844. |
| Non-code | Extends the 40/60 percentage of completion/capitalized cost method to naval shipbuilders. Allows naval shipbuilders to use this method of accounting, which was previously restricted to only certain ship construction contracts under the Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203). Applicable to contracts for ships or submarines with respect to which the construction commencement date occurs after October 22, 2004. Act §708. |

The following provisions are NOT operative for Hawaii income tax purposes.

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| § 38(b) | General business credit: Current year business credit. Makes conforming amendment - addition of a general business credit equal to 50 percent of the qualified railroad track maintenance expenditures paid or incurred in a taxable year. Effective for taxable years beginning after December 31, 2004. Act §245(c). |
| § 39(d) | Carryback and carryforward of unused credits: Transitional rules. Replaces the specific transitional rules in subsections (1) through (10) with one general transitional rule. Effective for taxable years beginning after December 31, 2003. Act §245(b). |
| § 40(g)(6) | Alcohol used as fuel: definitions and special rules for eligible small ethanol producer credit. Adds new subsection to allow cooperatives to elect to pass the small ethanol producer credit through to their patrons. Effective for taxable years ending after October 22, 2004. Act §313. |
| § 45 | Credit for electricity produced from certain renewable resources. Expands definitions of qualified energy resources and qualified facilities. Generally, applicable to electricity produced and sold after October 22, 2004 in taxable years beginning after October 22, 2004. Act §710. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 45D(e) | New markets tax credit. Modifies the definition of low-income community. Applicable for designations made after October 22, 2004 and investments made after October 22, 2004. Act §221. |
| § 45D(e) | New markets tax credit. Adds new subparagraph (5), "Modification of income requirement for census tracts within high migration rural counties." Effective as if included in the Community Renewal Tax Relief Act of 2000. Act §223. |
| § 45G | Railroad Track Maintenance Credit. Adds a general business credit equal to 50 percent of the qualified railroad track maintenance expenditures paid or incurred in a taxable year. Applicable to qualified expenditures paid or incurred during the taxable years beginning after December 31, 2004 and before January 1, 2008. Act §245. |
| § 45H | Credit for production of low sulfur diesel fuel. Adds a general business credit equal to five cents for each gallon of low sulfur diesel fuel produced during the taxable year by a small business refiner at such facility. Applicable to expenses paid or incurred after December 31, 2002 in taxable years ending after December 31, 2002. Act §339. |
| § 45I | Credit for producing oil and gas from marginal wells. Adds a general business credit equal to \$3 per barrel of qualified crude oil production and 50 cents per 1,000 cubic feet of qualified natural gas production. Applicable to production in taxable years beginning after December 31, 2004. Act §341. |
| § 55(c) | Alternative minimum tax: regular tax. Coordinates with income averaging for farmers and fisherman for AMT purposes by determining the regular tax liability, for AMT purposes, without regard to income averaging. Effective for taxable years beginning after December 31, 2003. Act §314(a). |
| § 56(g)(4)(B)(i) | Alternative minimum tax. Makes conforming amendment - repeal of IRC section 114: extraterritorial income. Applicable to transactions after December 31, 2004. Act §101(b)(4). |
| § 114 | Extraterritorial income. Repeals the exclusion, disallowance of deductions, and denial of credits for certain foreign taxes in connection with extraterritorial income. Applicable to transactions after December 31, 2004. Act §101(a). |
| § 168(k) | Accelerated cost recovery system: Special allowance for certain property acquired after September 10, 2001 and before January 1, 2005. Allows qualifying aircrafts to be eligible for the additional first-year depreciation deduction if the qualifying aircrafts are placed in service before January 1, 2006. Effective as if included in the Job Creation and Worker Assistance Act of 2002 Act §101. Act §336. |
| § 168(k)(2)(E)(iii) | Accelerated cost recovery system: Special allowance for certain property acquired after September 10, 2001 and before January 1, 2005. Provides special rule in the case of multiple units of property subject to the same lease. Applicable to property sold after June 4, 2004. Act §337. |
| § 179 | Election to expense certain depreciable business assets. Extends for an additional two years the increased amounts that a taxpayer may expense under (\$100,000 indexed for inflation) and other expensing enhancements so that they continue up to tax year 2007. Effective on October 22, 2004. Act §201. |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| § 179B | Deduction for capital costs incurred in complying with environmental protection agency sulfur regulations. Adds new section to allow small business refiners to immediately deduct as an expense up to 75 percent of the costs paid or incurred for the purpose of complying with the Highway Diesel Fuel Sulfur Control Requirements of the Environmental Protection Agency (EPA). Costs qualifying for the deduction are those costs paid or incurred with respect to any facility of a small business refiner during the period beginning on January 1, 2003, and ending on the earlier of the date that is one year after the date on which the taxpayer must comply with the applicable EPA regulations or December 31, 2009. For these purposes a small business refiner is a taxpayer who is in the business of refining petroleum products and employs not more than 1,500 employees directly in refining and has less than 205,000 barrels per day (average) of total refinery capacity. The deduction is reduced, pro rata, for taxpayers with capacity in excess of 155,000 barrels per day. Applicable to expenses paid or incurred after December 31, 2002, in taxable years ending after December 31, 2002. Act §338. |
| § 181 | Treatment of certain qualified film and television productions. Adds new section that allows qualifying film and television productions (any production of a motion picture (whether released theatrically or directly to video cassette or any other format) miniseries, scripted, dramatic television episode or movie of the week) to elect to deduct certain production expenditures in the year the expenditure is incurred in lieu of capitalizing and recovering it through depreciation allowances. Applicable to qualified film and television productions commencing after October 22, 2004 and before January 1, 2009. Act §244. |
| § 199 | <p>New deduction—the “U.S. production activities deduction.” A deduction equal to 9 percent on all manufacturing (and certain other domestic production) activity undertaken in the U.S., whether it is exported or not. The deduction is available to C corporations, S corporations, partnerships, sole proprietorships, cooperatives, and estates and trusts, and is allowed for AMT purposes. The deduction is phased in over five years: 3% in 2005-2006, 6% for 2007-2009, 9% after 2009.</p> <p>IRC § 199 replaces the exclusion of extraterritorial income. The IRC § 199 deduction is equal to a portion of a taxpayer’s qualified production activities income and is applicable to a very broad base of taxpayers and activities.</p> <p>Taxpayers whose products are primarily or exclusively consumed in the United States will receive the greatest benefit over the taxpayers who primarily exported products and benefited from the exclusion of extraterritorial income.</p> <p>Qualified production activities income includes:</p> <ol style="list-style-type: none">i. Income from any lease, rental, license, sale, exchange or other disposition of:ii. Qualifying production property (any tangible personal property, computer software, and any sound recordings) that was manufactured, produced, grown, or extracted by the taxpayer in whole or in significant part within the United States; oriii. Qualified film (any motion picture film or videotape, live or delayed television programming) produced by the taxpayer;iv. Income from any sale, exchange or other disposition of electricity, natural gas, or potable water produced by the taxpayer within the United States;v. Construction activities performed in the United States; or |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| | <p>vi. Engineering or architectural services performed in the United States;</p> <p>vii. Agricultural products;</p> <p>viii. Food processing; or</p> <p>ix. Food products if such food products were not prepared and sold at retail at the taxpayer's retail establishment.</p> <p>Effective for tax years beginning after December 31, 2004. Act §102.</p> |
| § 501(c)(12) | <p>Exemption from tax on corporations, certain trusts, etc.: list of exempt organizations - benevolent life insurance associations of a purely local character, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations. Amends exemption provisions. Effective for taxable years beginning after October 22, 2004. Act §§ 319(a) and (b).</p> |
| §864(e)(3) | <p>Definitions and special rules: rules for allocating interest, etc. - tax exempt assets not taken into account. Makes conforming amendment - repeal of IRC section 114: extraterritorial income. Applicable to transactions after December 31, 2004. Act §101(b)(6).</p> |
| §864 | <p>Definitions and special rules: election to allocate interest, etc. on worldwide basis.</p> <ol style="list-style-type: none">1. Redesignates subsection (f) as (g);2. Adds new subsection (f) to allow for an election to allocate interest on worldwide basis; and3. Amends subsection (e)(7) to add new subparagraph (F). <p>Effective for taxable years beginning after December 31, 2008. Act §401.</p> |
| §903 | <p>Credit for taxes in lieu of income, etc., taxes. Makes conforming amendment - repeal of IRC section 114: extraterritorial income. Applicable to transactions after December 31, 2004. Act §101(b)(7).</p> |
| §904 | <p>Limitation on credit:: Recharacterization of overall domestic loss; Look-thru rules to apply to dividends from noncontrolled section 902 corporations; Reduction to 2 foreign tax credit baskets.</p> <ol style="list-style-type: none">1. Redesignates subsections (g), (h), (i), (j), and (k) as subsections (h), (i), (j), (k), and (l);2. Adds new subsection (g) recharacterization of overall domestic loss; and3. Amends subsection (d). <p>Generally, applicable to: losses for taxable years beginning after December 31, 2006; taxable years beginning after December 31, 2002; taxable years beginning after December 31, 2006. Act §§ 402, 403, and 404.</p> |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| §§ 941 - 943 | Subpart E of part III of subchapter N of chapter 1: Qualifying Foreign Trade Income. Repeals subpart E (conforming amendment - repeal of IRC section 114: extraterritorial income). Applicable to transactions after December 31, 2004. Act §101(b)(1). |
| § 965 | Temporary dividends received deduction. Allows for a temporary dividends received deduction as an incentive to reinvest foreign earnings in the United States. Effective for taxable years ending on or after October 22, 2004. Act §422. |
| §999(c)(1) | Reports by taxpayers; determinations: international boycott factor. Makes conforming amendment - repeal of IRC section 114: extraterritorial income. Applicable to transactions after December 31, 2004. Act §101(b)(8). |
| §§ 1352 - 1359 | Election to determine corporate tax on certain international shipping activities using per ton rate. Adds subchapter R that provides an alternative tax on qualifying shipping activities. Allows corporations to elect a "tonnage tax" in lieu of the U.S. corporate income tax on taxable income from international shipping activities. An electing corporation's gross income does not include its income from "qualifying shipping activities." Instead, an electing corporation is subject to tax on "qualifying shipping activities" only at the maximum corporate income tax rate on its "notional shipping income," which is based on the net tonnage of the corporation's vessels. Effective for taxable years beginning after Oct. 22, 2004. Act §248. |
| § 1400E | Designation of renewal communities. Adds new subsection (g), "expansion of designated area based on 2000 census." Effective as if included in the Community Renewal Tax Relief Act of 2000 Act §101. Act §222. |
| Non-code | Phases-in the repeal of IRC section 114 for 2005 and 2006 by including as gross income an amount not to exceed 20% and 40% of the extraterritorial income, respectively. Allows for the revocation of the election made under IRC section 943(e) during the period of October 22, 2004 through October 21, 2005. The repeal of IRC section 114 does not apply to transactions occurring under qualified binding contracts. Applicable to transactions after December 31, 2004. Act §§101(d), (e), and (f). |

Digest of the Pension Funding Equity Act of 2004

(P. L. No. 108-218, April 10, 2004)

Note: Only amendments or additions to Internal Revenue Code Sections contained in subtitle A, chapter 1, and certain 6000 series sections of the Internal Revenue Code of 1986, as amended, are applicable for this Digest.

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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The following provisions are operative for Hawaii income tax purposes.

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| §404(a)(1) | Deduction for contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan: general rule - pension trusts. Provides an election to disregard modified interest rate provisions (new permissible range of interest rates) in IRC §§ 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) solely for purposes of determining the interest rate used in calculating the maximum amount of the deduction allowable. Effective for plan years beginning after December 31, 2003. Act §101(b)(5). |
| §412(b)(5)(B) | Minimum funding standards: funding standard account - interest. Temporarily replaces the 30-year Treasury rate with a rate based on long-term corporate bonds for determining the plan's current liability for funding and deduction purposes. Also makes conforming amendments. Effective for plan years beginning after December 31, 2003 and before January 1, 2006. Act §101(b)(1). |
| §412(b)(7) | Minimum funding standards: funding standards account – special rules for multiemployer plans – election for deferral of charge for portion of net experience loss. With respect to multi-employer plans, allows the plan sponsor to elect to defer up to 80% of certain charges attributable to the amortization of a net experience loss for the first post-2001 plan year. Applicable to deferral elections made for any plan year beginning after June 30, 2003 and before July 1, 2005 in which the deferral is charged to any plan year selected by the plan from either of the two immediately succeeding plan years. Act §104(b). |
| §412(l)(7)(C)(i) | Minimum funding standards: additional funding requirements for plans which are not multiemployer plans - current liability - interest rate and mortality assumptions used – interest rate – special rule for 2004 and 2005. Temporarily replaces the 30-year Treasury rate with a rate based on long-term corporate bonds for determining the plan's current liability for funding and deduction purposes. Effective for plan years beginning after December 31, 2003 and before January 1, 2006. Act §101(b)(2). |
| §412(l)(12) | Minimum funding standards: additional funding requirements for plans which are not multiemployer plans - election for certain plans. With respect to single-employer defined benefit plans, allows commercial passenger airlines, steel companies, and one particular tax-exempt IRC § 501(c)(5) organization to elect to make reduced additional required charges for any two plan years beginning after December 27, 2003, and before December 28, 2005, if such plan was not subject to the deficit reduction contribution rules for the plan year beginning in 2000. Act §102(b). |

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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| §412(m)(7) | Minimum funding standards: quarterly contributions required - special rule for 2002. Makes conforming amendments in connection with temporarily replacement of the 30-year Treasury rate with a rate based on long-term corporate bonds. Effective for plan years beginning after December 31, 2003 and before January 1, 2006. Act §101(b)(3). |
| §415(b)(2)(E)(ii) | Limitations on benefits and contributions under qualified plans: limitation for defined benefit plans - annual benefit – limitation on certain assumptions. Adds new provision that substitutes the applicable interest rate of 5 percent with 5.5 percent. Effective for plan years beginning after December 31, 2003 and before January 1, 2006. Act §101(b)(4). |
| §420(b)(5) | Transfers of excess pension assets to retiree health accounts: qualified transfer - expiration. Extends the sunset date so that transfers made after December 31, 2013 shall not be treated as "qualified transfers." Effective on April 10, 2004. Act §204(a). |
| Non-code | Provisions relating to plan amendments. With respect to any plan or annuity contract amendment made, during the first plan year beginning on or after January 1, 2006, in connection with §101 of the Act, provides retroactive plan amendment relief if the plan or contract was operated as if such amendment was in effect during the period beginning on the date the amendment takes effect and ending on the earlier of the date the amendment was adopted or the last day of the first plan year beginning on or after January 1, 2006. Act §101(c). |
| Non-code | Lookback rules. Provides a "lookback" rule for purposes of applying the following provisions to plan years beginning after December 31, 2003: (1) IRC § 412(l)(9)(B)(ii), regarding the "volatility rule" exception to the determination of a plan's funded current liability percentage; and (2) IRC § 412(m)(1), regarding the rule where quarterly contributions are required for a plan year if the plan's funded current liability percentage was less than 100% for the preceding plan year. For these purposes, the temporary replacement of the 30-year Treasury bond rate with the corporate bond rate may be retroactively applied as if the changes had been in effect for all prior years. Effective on April 10, 2004. Act §101(d)(2). |
| Non-code | Transition rule for IRC § 415 limitation. With respect to distributions made after December 31, 2003 and before January 1, 2005, the amount payable under any form of benefit subject to IRC § 417(e)(3) and subject to adjustment under IRC § 415(b)(2)(B) shall not, solely by reason of IRC § 415(b)(4), be less than the amount that would have been so payable had the amount payable been determined using the applicable interest rate in effect as of the last day of the last plan year beginning before January 1, 2004. Effective on April 10, 2004. Act §101(d)(3). |
| Non-code | Two-year extension of transition rule to pension funding requirements. Modifies the transitional relief, for 2004 and 2005, for plans sponsored by any company engaged primarily in interurban or interstate passenger bus service. The funded current liability percentage is treated, for 2004 and 2005, as: 1. At least 90% for purposes of determining the amount of required contributions under IRC § 412(l)(9)(A); and |

CODE SECTION DESCRIPTION OF PROVISION

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| | 2. 100% for purposes of determining whether quarterly contributions are required under IRC § 412(m). |
| Non-code | Effective for plan years beginning after December 31, 2003. Act §201. Procedures applicable to disputes involving pension plan withdrawal liability. Adds special rules that apply to pension plan withdrawal liability disputes. Applicable to any employer that receives a notification of withdrawal liability under ERISA § 4219(b)(1) after October 31, 2003. Act §202. |

The following provisions are NOT operative for Hawaii income tax purposes.

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| §501(c)(15) | Exemption from tax on corporations, certain trusts, etc.: list of exempt organizations. Limits the tax-exempt eligibility of small property and casualty insurance companies. Effective for taxable years beginning after December 31, 2003. Act §206. |
| §807 | Rules for certain reserves. Makes conforming amendments in connection with the repeal of IRC §809. Effective for taxable years beginning after December 31, 2004. Act §205. |
| §808(c) | Policyholder dividends deduction – amount of deduction. Provides that the deduction for policyholder dividends for any taxable year will be equal to the policyholder dividends paid or accrued during the taxable year. Effective for taxable years beginning after December 31, 2004. Act §205. |
| §809 | Reduction in certain deductions of mutual life insurance companies. Repeals this section in the entirety. Effective for taxable years beginning after December 31, 2004. Act §205. |
| §812 | Definition of company's share and policyholders' share. Makes conforming amendments in connection with the repeal of IRC §809. Effective for taxable years beginning after December 31, 2004. Act §205. |
| §817 | Treatment of variable contracts. Makes conforming amendments in connection with the repeal of IRC §809. Effective for taxable years beginning after December 31, 2004. Act §205. |
| §831 | Tax on insurance companies other than life insurance companies. Adds definition of insurance company. Makes conforming amendment in connection with the amendment to IRC §501(c)(15). Effective for taxable years beginning after December 31, 2003. Act §206. |
| §842 | Foreign companies carrying on insurance business. Makes conforming amendments in connection with the repeal of IRC §809. Effective for taxable years beginning after December 31, 2004. Act §205. |

Digest of An Act to Accelerate the Income Tax Benefits for Charitable Cash Contributions for the Relief of Victims of the Indian Ocean Tsunami (P. L. No. 109-001, January 7, 2005)

Note: Only amendments or additions to Internal Revenue Code Sections contained in subtitle A, chapter 1, and certain 6000 series sections of the Internal Revenue Code of 1986, as amended, are applicable for this Digest.

| <u>CODE SECTION</u> | <u>DESCRIPTION OF PROVISION</u> |
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The following provisions are operative for Hawaii income tax purposes.

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| Non-code | Although H.R. 241 (P.L. 109-001) was enacted on January 7, 2005, the purpose of §§ 235-2.5(c) and 235-3, HRS, is broad enough to include the provisions of P.L. 109-001 in Act 60, Session Laws of Hawaii 2005. P.L. 109-001 allows taxpayers to treat qualified charitable cash contributions that were made in January 2005 for the relief of victims in areas affected by the December 26, 2004 Indian Ocean tsunami as if such contributions were made on December 31, 2004, and not in January 2005, for purposes of IRC § 170. |
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Taxpayers who may benefit from the provisions of P.L. 109-001 are (a) individuals who itemize their deductions and (b) other calendar year taxpayers.

To qualify for the accelerated deduction, all four criteria must be met:

1. The charitable contribution must be in the form of cash. Marketable securities and other property do NOT qualify for purposes of P.L. 109-001. Charitable contributions made by (a) check are treated as cash contributions and (b) credit card are treated as cash contributions made at the time of the credit card charge;
2. The charitable cash contribution must be made in January 2005 (after December 31, 2004 and before February 1, 2005);
3. The charitable cash contribution must be paid to an eligible charitable organization whose program(s) support relief operations in the Indian Ocean basin (e.g., programs that help to eliminate the burden of shipping goods overseas and stimulate the economic growth by generating more cash flow in the Indian Ocean basin's economies); and
4. The charitable cash contribution must be pledged and fully earmarked to aid victims in areas affected by the December 26, 2004 Indian Ocean tsunami, for which a charitable contribution deduction is allowed under IRC § 170. The taxpayer must have records to substantiate that the charitable cash contribution was pledged and fully earmarked to provide the aforementioned aid.

The following contributions do NOT qualify for purposes of P.L. 109-001:

1. Charitable contributions to foreign organizations;
2. Charitable contributions pledged, earmarked, or used to fund programs that do

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not solely provide Indian Ocean tsunami-related disaster relief; or

3. Non-cash charitable contributions such as marketable securities and other property contributions.

Taxpayers may choose to deduct qualified charitable cash contributions for either (a) the 2004 tax year or (b) the 2005 tax year. Multiple contributions may be treated as separate contributions for purposes of this allocation. However, the qualified charitable cash contribution can only be deducted once. Taxpayers claiming a deduction for the 2004 tax year with respect to the qualified charitable cash contribution shall NOT claim a deduction for the 2005 tax year with respect to the same contribution.

For more information on the qualified charitable cash contributions, please refer to the following news releases and publications:

- (1) The United States Senate Committee on Finance news releases dated January 12, 2005 and January 19, 2005;
- (2) Internal Revenue Service (IRS) News Release IR-2005-06, New Law Encourages Tsunami Relief Contributions, dated Jan. 10, 2005;
- (3) IRS Publication 78, Cumulative List of Organizations described in Section 170(c) of the Internal Revenue Code of 1986;
- (4) IRS Publication 526, Charitable Contributions; and
- (5) IRS Publication 3833, Disaster Relief: Providing Assistance through Charitable Organizations.

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