

### HOUSE WAYS AND MEANS COMMITTEE APPROVES THE AMERICAN JOBS CREATION ACT INCLUDING NEW DEFERRED COMPENSATION RULES

June 15, 2004

*On June 14, 2004, the House Ways and Means Committee approved, by a bi-partisan vote of 27-9, the American Jobs Creation Act of 2004 ("AJCA") (H.R. 4520), which includes new nonqualified deferred compensation rules similar to those included in the Jumpstart our Business Strength Act ("JOBS") (S. 1637) that was approved by the full Senate on May 11, 2004 (see our Bulletins Nos. 04-82, 04-77 and 04-64). The next step is consideration of AJCA by the House, which may occur as early as June 18, 2004. Following expected approval by the House, the two bills would have to be reconciled by a conference committee, a process certain staffers on the Hill believe may be completed as early as the end of July.*

The two bills are primarily focused on the repeal of the U.S. export tax regime in response to a 2002 World Trade Organization ruling. Until that repeal is accomplished, certain U.S. exports will be subject to escalating sanctions from the European Union. Because of these political and economic factors, it is likely that this legislation will be enacted in this session of Congress. In addition, because the nonqualified deferred compensation provisions have been scored as generating almost \$900 million in revenue over a 10-year period, it is likely that, if the export bills are passed, they will include those provisions.

Although the deferred compensation treatments in the two bills are similar, there are a number of significant differences which will have to be reconciled in the conference committee. In addition, the AJCA includes a retroactive effective date (i.e., generally applicable to compensation deferred after June 3, 2004) and the JOBS bill would generally be effective beginning in 2005. These effective date provisions could create significant compliance issues for existing arrangements.

In connection with the House Ways and Means Committee's consideration of AJCA, the Joint Committee on Taxation ("JCT") issued an explanation which "clarified" certain aspects of the proposed legislation.

For example, as passed by Ways and Means, the AJCA is generally effective for compensation deferred after June 3, 2004. In addition, unlike the JOBS bill, the AJCA includes a grandfather rule which provides that the new rules would not apply to amounts deferred after June 3, 2004, and before January 1, 2005, pursuant to an irrevocable election or binding arrangement made before June 4, 2004. The JCT explanation

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indicates that amounts "further deferred" under a subsequent election will be subject to the new rules. As a result, deferred compensation that would not be subject to the new rules because it was deferred before the general effective date (or pursuant to a grandfather election) would lose its "grandfather" treatment if the compensation is re-deferred to a later date. It is not necessarily clear what "further deferred" may mean in all cases for this purpose. For example, if a current arrangement allows participants to select the form of distribution at some point in the future (e.g., between a lump sum and installments), it is not clear whether the election of installments would be considered a further deferral. In addition, it is not clear whether other modifications to an arrangement would jeopardize its grandfather status.

Furthermore, the two bills would require that the initial deferral election must generally be made before the calendar year in which the services are performed. Although the proposed legislation does not expressly address when the time and form of distributions must initially be specified, the JCT explanation provides that such designations must be made at the time of the initial deferral. As a result, participants will no longer be able to elect the form of distribution at a later date (e.g., one year prior to the scheduled commencement date). However, the proposed legislation expressly allows participants to "change" the timing and form of distribution so long as the change is made at least 12 months prior to the first scheduled payment date and the new payment date is extended at least 5 years.