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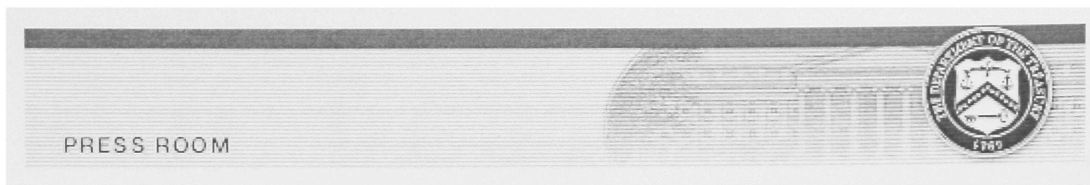
Department of the Treasury

PRESS RELEASES

The following numbers were not used:

JS-1105, 1140, and 1141.
For JS-1081 see 1084.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 2, 2004
js-1077

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky Regarding December Purchasing Managers' Index

Today's Purchasing Managers' Index report suggests progress in manufacturing. December's index was above the "breakeven" 50 level for the sixth straight month and at the highest level in twenty years. The new orders index posted the strongest showing in over fifty years. The report also suggests a better employment picture -- further evidence the President's initiatives are creating economic growth and boosting job creation. However, there is more to be done and this Administration will continue its efforts until every American looking for work can find a job.

-30-

FROM THE OFFICE OF PUBLIC AFFAIRS

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To view or print the Microsoft Word content on this page, download the free Microsoft Word Viewer.

January 6, 2004
JS-1078

Media Advisory: Secretary Snow Will Host G-7 Meeting in February

U.S. Treasury Secretary John W. Snow will host a meeting of the G-7 Finance Ministers and Central Bank Governors on Friday, Feb. 6 and Saturday, Feb. 7 in Boca Raton, Florida at the Boca Raton Resort and Club.

Media planning to cover the meeting will be required to register. Information on registration and accommodations is attached below.

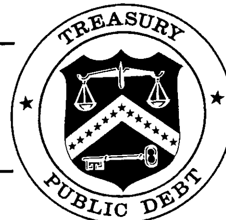
Further details regarding the G-7 meeting will be forthcoming. Treasury Public Affairs contacts are Tony Fratto, 202-622-2910, and Betsy Holahan, 202-622-1997

Related Documents:

- Media Registration Form (Word)
- Media Registration Form (PDF)
- Local Overflow Hotels

PUBLIC DEBT NEWS

Department of the Treasury • Bureau of the Public Debt • Washington, DC 20239



TREASURY SECURITY AUCTION RESULTS
BUREAU OF THE PUBLIC DEBT - WASHINGTON DC

FOR IMMEDIATE RELEASE
January 05, 2004

CONTACT: Office of Financing
202-691-3550

RESULTS OF TREASURY'S AUCTION OF 26-WEEK BILLS

Term:	182-Day Bill
Issue Date:	January 08, 2004
Maturity Date:	July 08, 2004
CUSIP Number:	912795QS3

High Rate: 1.020% Investment Rate 1/: 1.043% Price: 99.484

All noncompetitive and successful competitive bidders were awarded securities at the high rate. Tenders at the high discount rate were allotted 35.48%. All tenders at lower rates were accepted in full.

AMOUNTS TENDERED AND ACCEPTED (in thousands)

Tender Type	Tendered	Accepted
Competitive	$ 32,982,905	$ 15,061,565
Noncompetitive	908,485	908,485
FIMA (noncompetitive)	30,000	30,000
SUBTOTAL	33,921,390	16,000,050 2/
Federal Reserve	5,783,469	5,783,469
TOTAL	$ 39,704,859	$ 21,783,519

Median rate 1.005%: 50% of the amount of accepted competitive tenders was tendered at or below that rate. Low rate 0.990%: 5% of the amount of accepted competitive tenders was tendered at or below that rate.

Bid-to-Cover Ratio = 33,921,390 / 16,000,050 = 2.12

1/ Equivalent coupon-issue yield.
2/ Awards to TREASURY DIRECT = $695,500,000

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PUBLIC DEBT NEWS

Department of the Treasury • Bureau of the Public Debt • Washington, DC 20239

TREASURY SECURITY AUCTION RESULTS
BUREAU OF THE PUBLIC DEBT - WASHINGTON DC

FOR IMMEDIATE RELEASE
January 05, 2004

CONTACT: Office of Financing
202-691-3550

RESULTS OF TREASURY'S AUCTION OF 13-WEEK BILLS

Term:	91-Day Bill
Issue Date:	January 08, 2004
Maturity Date:	April 08, 2004
CUSIP Number:	912795PT2

High Rate: 0.920% Investment Rate 1/: 0.939% Price: 99.767

All noncompetitive and successful competitive bidders were awarded securities at the high rate. Tenders at the high discount rate were allotted 9.33%. All tenders at lower rates were accepted in full.

AMOUNTS TENDERED AND ACCEPTED (in thousands)

Tender Type	Tendered	Accepted
Competitive	$ 37,873,517	$ 15,224,967
Noncompetitive	1,458,320	1,458,320
FIMA (noncompetitive)	316,800	316,800
SUBTOTAL	39,648,637	17,000,087 2/
Federal Reserve	5,976,563	5,976,563
TOTAL	$ 45,625,200	$ 22,976,650

Median rate 0.910%: 50% of the amount of accepted competitive tenders was tendered at or below that rate. Low rate 0.900%: 5% of the amount of accepted competitive tenders was tendered at or below that rate.

Bid-to-Cover Ratio = 39,648,637 / 17,000,087 = 2.33

1/ Equivalent coupon-issue yield.
2/ Awards to TREASURY DIRECT = $1,207,307,000

5 - 1080

DEPARTMENT OF THE TREASURY

TREASURY NEWS

OFFICE OF PUBLIC AFFAIRS • 1500 PENNSYLVANIA AVENUE, N.W. • WASHINGTON, D.C. • 20220 • (202) 622-2960

EMBARGOED UNTIL 11:00 A.M.
January 5, 2004

CONTACT: Office of Financing
202/691-3550

TREASURY OFFERS 5-YEAR NOTES

The Treasury will auction $16,000 million of 5-year notes to raise new cash.

Up to $1,000 million in noncompetitive bids from Foreign and International Monetary Authority (FIMA) accounts bidding through the Federal Reserve Bank of New York will be included within the offering amount of the auction. These noncompetitive bids will have a limit of $100 million per account and will be accepted in the order of smallest to largest, up to the aggregate award limit of $1,000 million.

The auction will be conducted in the single-price auction format. All competitive and noncompetitive awards will be at the highest yield of accepted competitive tenders. The allocation percentage applied to bids awarded at the highest yield will be rounded up to the next hundredth of a whole percentage point, e.g., 17.13%.

The notes being offered today are eligible for the STRIPS program.

This offering of Treasury securities is governed by the terms and conditions set forth in the Uniform Offering Circular for the Sale and Issue of Marketable Book-Entry Treasury Bills, Notes, and Bonds (31 CFR Part 356, as amended).

Details about the new security are given in the attached offering highlights.

oOo

Attachment

JS 1081

HIGHLIGHTS OF TREASURY OFFERING TO THE PUBLIC OF
5-YEAR NOTES TO BE ISSUED JANUARY 15, 2004

January 5, 2004

Offering Amount .... $16,000 million
Maximum Award (35% of Offering Amount) .... $ 5,600 million
Maximum Recognized Bid at a Single Yield .... $ 5,600 million
NLP Reporting Threshold .... $ 5,600 million

Description of Offering:
Term and type of security .... 5-year notes
Series D-2009
CUSIP number .... 912828 BV 1
Auction date .... January 7, 2004
Issue date .... January 15, 2004
Dated date .... January 15, 2004
Maturity date .... January 15, 2009
Interest rate .... Determined based on the highest accepted competitive bid
Yield .... Determined at auction
Interest payment dates .... July 15 and January 15
Minimum bid amount and multiples $1,000
Accrued interest payable by investor .... None
Premium or discount .... Determined at auction

STRIPS Information:
Minimum amount required $1,000
Corpus CUSIP number .... 912820 JS 7
Due date(s) and CUSIP number(s)
for additional TINT(s) .... See chart below

5-Year Note Due Dates and CUSIP Numbers for Additional TINTS

	2007	2008	2009
January 15	912833 C3 2	912833 C5 7	912833 C7 3
July 15	912833 C4 0	912833 C6 5	---

Submission of Bids:
Noncompetitive bids:
Accepted in full up to $5 million at the highest accepted yield.
Foreign and International Monetary Authority (FIMA) bids: Noncompetitive bids submitted through the Federal Reserve Banks as agents for FIMA accounts. Accepted in order of size from smallest to largest with no more than $100 million awarded per account. The total noncompetitive amount awarded to Federal Reserve Banks as agents for FIMA accounts will not exceed $1,000 million. A single bid that would cause the limit to be exceeded will be partially accepted in the amount that brings the aggregate award total to the $1,000 million limit. However, if there are two or more bids of equal amounts that would cause the limit to be exceeded, each will be prorated to avoid exceeding the limit.
Competitive bids:
(1) Must be expressed as a yield with three decimals, e.g., 7.123%.
(2) Net long position for each bidder must be reported when the sum of the total bid amount, at all yields, and the net long position equals or exceeds the NLP reporting threshold stated above.
(3) Net long position must be determined as of one half-hour prior to the closing time for receipt of competitive tenders.

Receipt of Tenders:
Noncompetitive tenders:
Prior to 12:00 noon eastern standard time on auction day
Competitive tenders:
Prior to 1:00 p.m. eastern standard time on auction day

Payment Terms: By charge to a funds account at a Federal Reserve Bank on issue date, or payment of full par amount with tender. *TreasuryDirect* customers can use the Pay Direct feature which authorizes a charge to their account of record at their financial institution on issue date.

DEPARTMENT OF THE TREASURY

TREASURY NEWS

OFFICE OF PUBLIC AFFAIRS • 1500 PENNSYLVANIA AVENUE, N.W. • WASHINGTON, D.C. • 20220 • (202) 622-2960

EMBARGOED UNTIL 11:00 A.M.
January 5, 2004

CONTACT: Office of Financing
202/691-3550

TREASURY OFFERS 10-YEAR INFLATION-INDEXED NOTES

The Treasury will auction $12,000 million of 10-year inflation-indexed notes to raise new cash.

Up to $1,000 million in noncompetitive bids from Foreign and International Monetary Authority (FIMA) accounts bidding through the Federal Reserve Bank of New York will be included within the offering amount of the auction. These noncompetitive bids will have a limit of $100 million per account and will be accepted in the order of smallest to largest, up to the aggregate award limit of $1,000 million.

The auction will be conducted in the single-price auction format. All competitive and noncompetitive awards will be at the highest yield of accepted competitive tenders. The allocation percentage applied to bids awarded at the highest yield will be rounded up to the next hundredth of a whole percentage point, e.g., 17.13%.

The notes being offered today are eligible for the STRIPS program.

This offering of Treasury securities is governed by the terms and conditions set forth in the Uniform Offering Circular for the Sale and Issue of Marketable Book-Entry Treasury Bills, Notes, and Bonds (31 CFR Part 356, as amended).

Details about the security are given in the attached offering highlights.

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Attachment

JS 1082

HIGHLIGHTS OF TREASURY OFFERING TO THE PUBLIC OF
10-YEAR INFLATION-INDEXED NOTES TO BE ISSUED JANUARY 15, 2004

January 5, 2004

Offering Amount ....$12,000 million
Maximum Award (35% of Offering Amount) ....$ 4,200 million
Maximum Recognized Bid at a Single Yield ....$ 4,200 million
NLP Reporting Threshold ....$ 4,200 million

Description of Offering:
Term and type of security ....10-year inflation-indexed notes
Series A-2014
CUSIP number ....912828 BW 9
Auction date ....January 8, 2004
Issue date ....January 15, 2004
Dated date ....January 15, 2004
Maturity date ....January 15, 2014
Interest rate ....Determined based on the highest accepted competitive bid
Real yield ....Determined at auction
Interest payment dates ....July 15 and January 15
Minimum bid amount and multiples $1,000
Accrued interest ....None
Premium or discount ....Determined at auction

STRIPS Information:
Minimum amount required $1,000
Corpus CUSIP number ....912820 JT 5
Due date(s) and CUSIP number(s)
for additional TIIN(s) ....January 15, 2014 - - 912833 C8 1

Submission of Bids:
Noncompetitive bids: Accepted in full up to $5 million at the highest accepted yield.
Foreign and International Monetary Authority (FIMA) bids: Noncompetitive bids submitted through the Federal Reserve Banks as agents for FIMA accounts. Accepted in order of size from smallest to largest with no more than $100 million awarded per account. The total noncompetitive amount awarded to Federal Reserve Banks as agents for FIMA accounts will not exceed $1,000 million. A single bid that would cause the limit to be exceeded will be partially accepted in the amount that brings the aggregate award total to the $1,000 million limit. However, if there are two or more bids of equal amounts that would cause the limit to be exceeded, each will be prorated to avoid exceeding the limit.
Competitive bids:
(1) Must be expressed as a real yield with three decimals, e.g., 3.123%.
(2) Net long position for each bidder must be reported when the sum of the total bid amount, at all yields, and the net long position equals or exceeds the NLP reporting threshold stated above.
(3) Net long position must be determined as of one half-hour prior to the closing time for receipt of competitive tenders.

Receipt of Tenders:
Noncompetitive tenders: Prior to 12:00 noon eastern standard time on auction day.
Competitive tenders: Prior to 1:00 p.m. eastern standard time on auction day.

Payment Terms: By charge to a funds account at a Federal Reserve Bank on issue date, or payment of full par amount with tender. *TreasuryDirect* customers can use the Pay Direct feature which authorizes a charge to their account of record at their financial institution on issue date.

Indexing Information:
CPI Base Reference Period 1982-1984
Ref CPI 01/15/2004 ....184.77419
Index Ratio 01/15/2004 ....1.00000

DEPARTMENT OF THE TREASURY

TREASURY NEWS

OFFICE OF PUBLIC AFFAIRS • 1500 PENNSYLVANIA AVENUE, N.W. • WASHINGTON, D.C. • 20220 • (202) 622-2960

EMBARGOED UNTIL 11:00 A.M.
January 5, 2004

Contact: Office of Financing
202/691-3550

TREASURY OFFERS 4-WEEK BILLS

The Treasury will auction 4-week Treasury bills totaling $9,000 million to refund an estimated $15,001 million of publicly held 4-week Treasury bills maturing January 8, 2004, and to pay down approximately $6,001 million.

Tenders for 4-week Treasury bills to be held on the book-entry records of *TreasuryDirect* will not be accepted.

The Federal Reserve System holds $15,517 million of the Treasury bills maturing on January 8, 2004, in the System Open Market Account (SOMA). This amount may be refunded at the highest discount rate of accepted competitive tenders in this auction up to the balance of the amount not awarded in today's 13-week and 26-week Treasury bill auctions. Amounts awarded to SOMA will be in addition to the offering amount.

Up to $1,000 million in noncompetitive bids from Foreign and International Monetary Authority (FIMA) accounts bidding through the Federal Reserve Bank of New York will be included within the offering amount of the auction. These noncompetitive bids will have a limit of $100 million per account and will be accepted in the order of smallest to largest, up to the aggregate award limit of $1,000 million.

The allocation percentage applied to bids awarded at the highest discount rate will be rounded up to the next hundredth of a whole percentage point, e.g., 17.13%.

This offering of Treasury securities is governed by the terms and conditions set forth in the Uniform Offering Circular for the Sale and Issue of Marketable Book-Entry Treasury Bills, Notes, and Bonds (31 CFR Part 356, as amended).

Details about the new security are given in the attached offering highlights.

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Attachment

JS-1083

PUBLIC DEBT NEWS

Department of the Treasury • Bureau of the Public Debt • Washington, DC 20239

TREASURY SECURITY AUCTION RESULTS
BUREAU OF THE PUBLIC DEBT - WASHINGTON DC

FOR IMMEDIATE RELEASE
January 06, 2004

CONTACT: Office of Financing
202-691-3550

RESULTS OF TREASURY'S AUCTION OF 4-WEEK BILLS

Term:	28-Day Bill
Issue Date:	January 08, 2004
Maturity Date:	February 05, 2004
CUSIP Number:	912795PJ4

High Rate: 0.850% Investment Rate 1/: 0.863% Price: 99.934

All noncompetitive and successful competitive bidders were awarded securities at the high rate. Tenders at the high discount rate were allotted 98.74%. All tenders at lower rates were accepted in full.

AMOUNTS TENDERED AND ACCEPTED (in thousands)

Tender Type	Tendered	Accepted
Competitive	$ 30,902,355	$ 8,966,380
Noncompetitive	33,732	33,732
FIMA (noncompetitive)	0	0
SUBTOTAL	30,936,087	9,000,112
Federal Reserve	3,757,258	3,757,258
TOTAL	$ 34,693,345	$ 12,757,370

Median rate 0.845%: 50% of the amount of accepted competitive tenders was tendered at or below that rate. Low rate 0.800%: 5% of the amount of accepted competitive tenders was tendered at or below that rate.

Bid-to-Cover Ratio = 30,936,087 / 9,000,112 = 3.44

1/ Equivalent coupon-issue yield.

JS-1085

HIGHLIGHTS OF TREASURY OFFERING
OF 4-WEEK BILLS TO BE ISSUED JANUARY 8, 2004

January 5, 2004

Offering Amount........................$ 9,000 million
Maximum Award (35% of Offering Amount)...$ 3,150 million
Maximum Recognized Bid at a Single Rate..$ 3,150 million
NLP Reporting Threshold.................$ 3,150 million
NLP Exclusion Amount....................$11,900 million

Description of Offering:
Term and type of security...........28-day bill
CUSIP number........................912795 PJ 4
Auction date........................January 6, 2004
Issue date..........................January 8, 2004
Maturity date.......................February 5, 2004
Original issue date.................August 7, 2003
Currently outstanding...............$45,707 million
Minimum bid amount and multiples....$1,000

Submission of Bids:
Noncompetitive bids: Accepted in full up to $1 million at the highest discount rate of accepted competitive bids.
Foreign and International Monetary Authority (FIMA) bids: Noncompetitive bids submitted through the Federal Reserve Banks as agents for FIMA accounts. Accepted in order of size from smallest to largest with no more than $100 million awarded per account. The total noncompetitive amount awarded to Federal Reserve Banks as agents for FIMA accounts will not exceed $1,000 million. A single bid that would cause the limit to be exceeded will be partially accepted in the amount that brings the aggregate award total to the $1,000 million limit. However, if there are two or more bids of equal amounts that would cause the limit to be exceeded, each will be prorated to avoid exceeding the limit.
Competitive bids:
(1) Must be expressed as a discount rate with three decimals in increments of .005%, e.g., 4.215%.
(2) Net long position (NLP) for each bidder must be reported when the sum of the total bid amount, at all discount rates, and the net long position equals or exceeds the NLP reporting threshold stated above.
(3) Net long position must be determined as of one half-hour prior to the closing time for receipt of competitive tenders.

Receipt of Tenders:
Noncompetitive tenders:
Prior to 12:00 noon eastern standard time on auction day
Competitive tenders:
Prior to 1:00 p.m. eastern standard time on auction day

Payment Terms: By charge to a funds account at a Federal Reserve Bank on issue date.

Bureau of the Public Debt
United States Department of the Treasury

ublic Debt Announces Activity for Securities in the STRIPS Program for ecember 2003

R IMMEDIATE RELEASE

uary 7, 2004

Bureau of the Public Debt announced activity for the month of December 2003, of securities within the Separate Trading of istered Interest and Principal of Securities program (STRIPS).

	In Thousands
icipal Outstanding (Eligible Securities)	$2,581,803,603
d in Unstripped Form	$2,407,109,550
d in Stripped Form	$174,694,053
onstituted in December	$12,634,252

ccompanying table, gives a breakdown of STRIPS activity by individual loan description. The balances in this table are subject to and subsequent revision. These monthly figures are included in Table V of the Monthly Statement of the Public Debt, entitled ings of Treasury Securities in Stripped Form."

TRIPS table, along with the new Monthly Statement of the Public Debt, is available on Public Debt's Internet site at: publicdebt.treas.gov. A wide range of information about the public debt and Treasury securities is also available at the site.

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U.S. Department of the Treasury, Bureau of the Public Debt

Last Updated September 27, 2004

S 1086

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 7, 2004
JS-1087

Prepared Remarks by Treasury Secretary John Snow
Delivered to the U.S. Chamber of Commerce
Wednesday, January 7, 2004

Thank you Tom [Donohue] for inviting me to join you today. I appreciate the opportunity to share with you our thoughts on how the economy is faring.

Let me take a moment to review some recent economic data.

Last week's report on December's Purchasing Managers' Index was the sixth straight month above 50 index points, showing solid growth in all of its components. December's reading was the highest in twenty years, led by new orders which reached its highest point in more than fifty years. These numbers suggest good progress in manufacturing.

Earlier this week the Commerce Department reported that construction spending in November set a record for the fifth month in a row, jumping 1.2 percent. Construction is up 15 percent in the past sixth months.

The housing sector has buoyed the economy over the past few years and continues to be a point of strength. Housing starts jumped to a twenty-year high in November contributing to a remarkable year in home building – possibly the best since 1978.

Industrial production grew by a strong 0.9 percent in November, the biggest monthly gain since 1999. Consumer goods and business equipment both increased and high-tech goods were especially strong, up 27.5 percent over last year.

Retail sales were up by a solid 0.9 percent in November, bolstered by strong auto sales. The holiday season appears to have ended well, with weekly reports showing a 5.6 percent increase in the most recent week, compared to a year ago.

Job creation continued in November, rising for the fourth straight month. In the last four months, over 300,000 jobs have been created, putting the economy on the right path -- the most robust four-month job growth record in nearly three years. Weekly unemployment claims have declined for the past three weeks, pushing the four-week moving average down to a near three-year low.

These recent encouraging signs suggest a sustainable economic recovery, building on a robust third quarter which saw real GDP growth of 8.2 percent – the best in nearly 20 years.

We are encouraged by these signs, but we are not satisfied.

Let me take a moment to discuss the President's vision, which without a doubt is the primary reason why the economy is improving.

This past May, the President signed the Jobs and Growth Tax Relief Reconciliation Act of 2003. The Act provided a boost to the economy this year, and it will provide a sound basis for promoting economic growth in the future. The Act will continue

to buoy the economy as taxpayers see increased tax refunds come April 15th from the increased child credit, reduced marriage penalty, and reduced rates, and as businesses invest to take advantage of the increased expensing and bonus depreciation.

This legislation was the right action to take, at precisely the right time. It directly helps families and workers. For example:

Taxpayers with children received an immediate boost from rebate checks of $400 per eligible child sent out in July and August.

Because of lower tax rates and less income tax withholding, workers saw higher take-home pay in their paychecks starting in July of this year.

Married couples benefit from reduction in the marriage penalty from expansion of the fifteen percent rate bracket, and an increase in the standard deduction for joint filers.

Families benefit from increased child tax credits.

Investors benefit from the lower tax rates on dividends and capital gains. These lower rates were a positive step toward the President's goal of reducing the double tax on dividends, and will help promote capital formation and an ownership society.

Small businesses are benefiting from a four-fold increase in the amount of new investment they can deduct in one year, from $25,000 to $100,000.

All businesses are benefiting from the increase in bonus depreciation from 30 to 50 percent, as well as its extension through 2004 (2005 for longer-lived property). This change addressed what had been a weak spot in the economic recovery – low corporate investment.

Now, consider the situation we might have without the President's tax plans. The Treasury Department ran an analysis on that scenario and the results were stark. Without the passage of the President's plans, by the second quarter in 2003, the unemployment rate would have been nearly 1 percentage point higher. As many as 1.5 million fewer Americans would be working, and real GDP would have been as much as 2 percent lower.
What's more, without the President's tax cuts, it is likely that by the end of 2004 the unemployment rate would be as much as 1.6 percentage points higher than it will be. Three million fewer Americans would be working, and real GDP would be as much as 3.5 to 4 percent lower.

Still, the labor markets aren't picking up as fast as we'd like to see. I can tell you that President Bush is not going to be satisfied with this recovery until every American who wants a job has one. We're not sitting back watching the numbers roll in – we're out there making this economy better – making conditions better for growth, investment, and job creation.
President Bush has unveiled a six-point plan to further strengthen this economy, and set us on a long-term path toward growth.

First, we are working to make health care more affordable and its costs more predictable, so employers can add new workers without also adding a large and uncertain burden of health care costs. We need to create an environment where health care spending is focused on providing high quality, high value care.

Second, we are working to prevent frivolous lawsuits from diverting money from job creation into legal battles. We also intend to ensure that when necessary lawsuits proceed, the settlements are paid to the victims, not the trial lawyers.

Third, we are working to build a more affordable, reliable energy system that can support the expansion of our economy.

Fourth, we are streamlining regulations and needless paperwork requirements that reduce business productivity and deter growth.

Fifth, we are opening new markets to high-value American products and bringing down prices for American consumers through trade agreements. Trade is a critical component of economic growth. The world economy is more connected than ever before, as a result of the dramatic expansion of trade and capital flows in recent decades. Financial markets are now closely integrated and businesses increasingly serve customers across the world. The United States stands ready to work with others who seek trade liberalization. On the matter of the importance of trade, here are some cold hard facts: trade benefits both emerging and industrial nations, trade leads to increased global prosperity, trade raises global standards of living, and trade creates jobs.

And sixth, we are working to make tax relief permanent, so businesses and families alike can plan for the future with confidence. This is one of the most critical parts of the President's agenda to strengthen the economy. Nothing will kill our prosperity faster than a repeal of the President's tax relief, which is scheduled to happen at the end of this decade if we don't take action now.

Consider this: if the 2001 and 2003 tax relief acts were to expire now, it would raise taxes by an average of $1,544 for 109 million taxpayers in 2003.

Let me be perfectly clear: failure to make the tax relief permanent would be a huge mistake and would put our recovery in jeopardy.

A key element of making tax relief permanent is making permanent the repeal of the death tax. The death tax falls on income that has already been taxed, sometimes twice before. It forces the destruction of thousands of small family businesses, and it discourages work, savings and asset-accumulation. It diverts resources into tax avoidance and enforcement that could be spent in economically productive activities.

Finally, a word about fiscal discipline. Our fiscal situation remains a matter of concern. With major expenditures to protect our nation's homeland security and fight the war on terror, coupled with a recovering economy, we still face a deficit in the $500 billion range for the current fiscal year -- larger than anyone wants. But that size deficit, at roughly 4.5% of GDP (compared with a modern peak of 6% during the 80s), is not historically out of range; and it is entirely manageable, if we continue the president's strong pro-growth economic policies and sound fiscal restraint. Indeed, with adoption of the President's policies, our projections show a solid path toward cutting the deficit in half, toward a size that is below 2% of GDP, within the next five years.

With renewed economic growth and Congress' cooperation in focusing spending on our most critical priorities, we can accomplish the great goals the President has set for the country, while dramatically improving our budget situation.

Thank you. I look forward to your questions.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 7, 2004
JS-1088

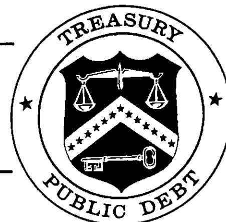
Statement from Acting Under Secretary for Domestic Finance, Brian Roseboro on the Report of the Working Group on Government Securities Clearance and Settlement

The Federal Reserve and the Working Group on Government Securities Clearance and Settlement have made a significant contribution to strengthen our government securities clearing system and, therefore, our financial system as a whole. The two existing major government securities clearing banks play an integral role in the government securities market, and the Working Group's report is an important part of the effort to ensure that the system is prepared in the event that the services of one of these two banks is disrupted or terminated.

The Treasury Department looks forward to continuing to work with the Federal Reserve, the SEC, other interested government agencies, and private sector participants to further strengthen the infrastructure of our government securities market.

PUBLIC DEBT NEWS

Department of the Treasury • Bureau of the Public Debt • Washington, DC 20239



TREASURY SECURITY AUCTION RESULTS
BUREAU OF THE PUBLIC DEBT - WASHINGTON DC

FOR IMMEDIATE RELEASE
January 07, 2004

CONTACT: Office of Financing
202-691-3550

RESULTS OF TREASURY'S AUCTION OF 5-YEAR NOTES

Interest Rate:	3 1/4%	Issue Date:	January 15, 2004
Series:	D-2009	Dated Date:	January 15, 2004
CUSIP No:	912828BV1	Maturity Date:	January 15, 2009

High Yield: 3.260% Price: 99.954

All noncompetitive and successful competitive bidders were awarded securities at the high yield. Tenders at the high yield were allotted 90.09%. All tenders at lower yields were accepted in full.

AMOUNTS TENDERED AND ACCEPTED (in thousands)

Tender Type	Tendered	Accepted
Competitive	$ 40,032,020	$ 15,898,848
Noncompetitive	101,176	101,176
FIMA (noncompetitive)	0	0
SUBTOTAL	40,133,196	16,000,024 1/
Federal Reserve	0	0
TOTAL	$ 40,133,196	$ 16,000,024

Median yield 3.240%: 50% of the amount of accepted competitive tenders s tendered at or below that rate. Low yield 3.200%: 5% of the amount accepted competitive tenders was tendered at or below that rate.

l-to-Cover Ratio = 40,133,196 / 16,000,024 = 2.51

Awards to TREASURY DIRECT = $61,484,000

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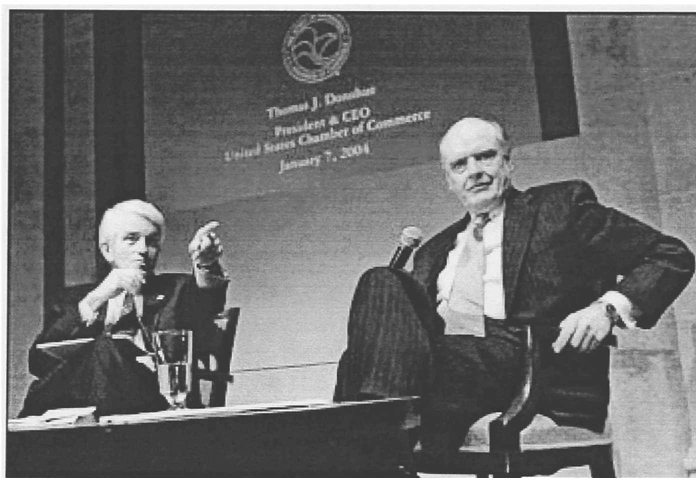
FROM THE OFFICE OF PUBLIC AFFAIRS

January 7, 2004
JS-1090

Secretary Snow Takes Questions from the Audience Following His Remarks on the Economy at the U.S. Chamber of Commerce



Media Contact

All media queries should be directed to
The Press Office at (202) 622-2960.
Only call this number if you are a member of the media.

High Resolution Image

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 8, 2004
js-1091

Remarks of Michael A. Dawson
Deputy Assistant Secretary
for
Critical Infrastructure Protection and Compliance Policy
at the Conference on
Protecting the Financial Sector and Cyber Security Risk Management
Organized by the
Federal Deposit Insurance Corporation
Minneapolis, Minnesota

"Protecting the Financial Sector from Terrorism and Other Threats"

I am here today because, unfortunately, terrorists continue to target the United States, its people, and its economy. In addition, we know that terrorists continue to target the financial infrastructure. The recent bombing, just before Thanksgiving, of a bank in Istanbul is a painful reminder of that fact. With over two hundred banks, credit unions, thrifts, securities firms, commodity futures merchants and insurance companies as well as a Federal Reserve Bank, Minneapolis is a significant hub of the financial infrastructure of the United States. You are the stewards of that financial infrastructure. I know you take the protection of this infrastructure very seriously. I thank you for your efforts.

The purpose of this conference is to share with you some of the policies and programs that may help you in this important task. In partnership with the FDIC, the Department of the Treasury and our colleagues in the public and private sectors are holding conference like this in twenty-four cities across the United States. During the conferences, we will reach thousands of professionals like you, stewards of our financial infrastructure. We hope you will take advantage of the policies and programs that you learn about today - policies and programs that can further strengthen the critical financial infrastructure of the United States.

Importance of Protecting Our Financial Infrastructure

The resiliency of the financial infrastructure is an issue that is very important to the Department of the Treasury. At the Treasury, we are responsible for developing and promoting policies that create jobs and improve the economy. We are also concerned with developing and promoting policies that enhance the resilience of the economy, policies that minimize the economic damage and speed economic recovery from a terrorist attack. Indeed, the President named Treasury as the lead agency to enhance the resilience of the critical financial infrastructure.

Fortunately, we are starting from a very strong base. The American economy is resilient. Over the past few years, we have seen that resilience first hand, as the American economy withstood a significant fall in equity prices, an economic recession, the terrorist attacks of September 11, corporate governance scandals, and the power outage of August 14-15. There are many reasons for the resilience of the American economy. Good policies - like the President's Jobs and Growth Initiative - played an important part. So has the resilience of the American people. One of the reasons are economy is so resilient is that our people are so tough, so determined to protect our way of life.

Like the economy as a whole, the American financial system is resilient. For example, the financial system performed extraordinarily well during the power outage last August. With one exception, the bond and major equities and futures markets were open the next day at their regular trading hours. Major market participants were also well prepared, having invested in contingency plans, procedures, and equipment such as backup power generators. The U.S. financial sector withstood this historic power outage without any reported loss or corruption of any customer data. This resilience mitigates the economic risks of terrorist attacks and other disruptions, both to the financial system itself and to the American economy as a whole.

Although we are starting from a strong base, the fact remains that terrorists continue to target the U.S. economy and U.S. financial institutions. Therefore, we must continue our vigilant efforts to protect our critical financial infrastructure.

Guiding Principles

Four principles guide our efforts to enhance the resilience of our financial infrastructure. These principles guided our actions as the financial system recovered from the attacks of September 11th. They guided our actions during the power outage of August 14-15. They guide our day to day actions as we prepare for the next disruption.

The first principle is to remember that the financial system is really about people. People, not buildings or computers, produce financial services. And it is people who benefit from financial services.

We depend on people to run the financial system. We need these people - tellers, technicians, loan officers, technologists - to see the system through times of stress. Indeed, it was the commitment of these professionals to their institutions, customers, and colleagues that helped the financial system recover from the attacks of September 11th and weather the power outage of August 14-15.

Just as we depend on people to run the financial system, people depend on the financial system to run. Every American depends on financial services to get their paycheck, buy their groceries, purchase a house, finance their children's education, or save for retirement. We must ensure that people continue to have confidence that the financial system will meet their needs.

The second principle is the importance of maintaining confidence. Confidence in the ability of financial institutions to clear checks, execute transactions, and satisfy insurance obligations helps the system weather significant disruption from evolving threats. By relying on a sound financial system, Americans can make business decisions for the future and

conduct necessary business in the present.

The third principle is to ensure that the financial system remains accessible and open for business when the safety of the employees permits. During times of disaster, investors depend on markets to price the impact of the disruption on assets. The longer markets are closed, the longer investors must go without knowing what the impact will be. This uncertainty can itself be harmful to the economy, compounding the impact of any disruption. The sooner we can eliminate this uncertainty, the more we can mitigate the impact and speed recovery.

Fourth, we want to promote responsible decision-making and problem-solving within the private sector. In general, financial institutions should make the appropriate decisions without waiting for guidance from Washington. After all, it is the private sector that owns and operates the majority of the financial systems. You in the private sector have the subject matter expertise in your own systems. It is the private sector that best knows how to help these systems recover from a disruption.

Organization

With these principles in mind, we have organized ourselves into two main groups. One is the Financial and Banking Information Infrastructure Committee (FBIIC). The FBIIC is sponsored by the President's Working Group on Financial Markets and consists of many state and federal regulators. The FDIC, which organized this conference today, is a member. So too are the Board of Governors of the Federal Reserve System, the Securities and Exchange Commission, the Commodity Futures Trading Commission, the National Association of Insurance Commissioners, the Conference of State Banking Supervisors, and many other important regulators. Treasury chairs the FBIIC.

The other important group is the Financial Services Sector Coordinating Council (FSSCC). The FSSCC consists of virtually every important financial services association in the United States.

The structure of these organizations advances the principles I just spoke about. As the President stated in his National Strategy for the Physical Protection of Critical Infrastructures and Key Assets, "it is important to remember that protection of our critical infrastructures and key assets is a shared responsibility. Accordingly, the success of our protective efforts will require close cooperation between government and the private sector at all levels." These two organizations facilitate that close cooperation and encourage private sector responsibility to protect the critical financial infrastructure without adding unnecessary layers of bureaucracy.

Policies

The four principles - protecting people, maintaining confidence, maintaining access to financial institutions, and promoting de-centralized decision-making and responsibility - shape our policies to enhance the resilience of the U.S. economy. For example, they highlight the importance of developing accurate and timely information about threats and sharing that information with the private sector. As we share more and better information about threats, people in the private sector who own and operate our financial infrastructure can better estimate the risks they bear and can more effectively reduce the probability of a disruption through strategic investments.

Furthermore, as more institutions invest in better security measures, the incentive for other firms to invest will also increase as they realize they might be left behind the competition. This tipping or cascading effect on businesses provides a very efficient and effective means of encouraging optimal investment in our corporate resilience. It also reduces the need for the government to impose costly, inflexible, and potentially ineffective command-and-control security regulations on the private sector.

Programs

I wish to highlight a few of the programs that we have developed. These programs provide you with specific, tangible services that can help make your institutions and your colleagues safer.

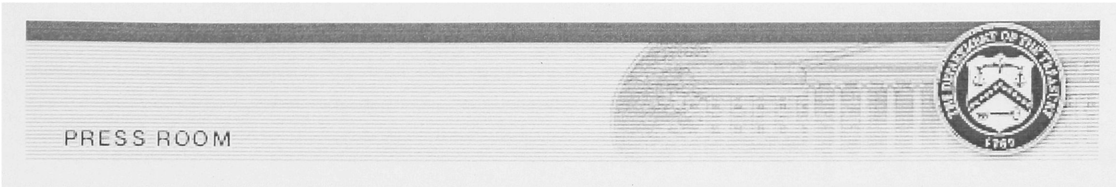
Recently, the FBIIC and the FSSCC launched the next generation Financial Services Information Sharing and Analysis Center (FS/ISAC). Since 1999, the FS/ISAC has been a leader in information sharing for the financial sector, allowing members to receive and submit anonymous reports on security threats and solutions. This next generation FS/ISAC includes both cyber and physical threat information; serves the entire sector; and deploys a secure, confidential technology platform where companies can exchange information in real time as they identify vulnerabilities, address the vulnerabilities, and respond to attempts to exploit the vulnerabilities.

Given the benefits of increased information sharing on the general public, Treasury is pleased to support the next-generation FS/ISAC. I hope that all of you will consider joining the FS/ISAC as members. You can learn more about how your financial institution can benefit from the FS/ISAC at www.fsisac.com.

Another important program is the Government Emergency Telecommunications Service (GETS) program. This program, which is run by the National Communications Service, provides critical members of the private sector priority access to the telecommunication system. In times of emergency when the telephone system experiences heavy traffic, GETS users can complete their calls faster so that they may discuss and coordinate emergency decisions. The importance of this emergency tool is apparent. Therefore, it is no surprise that since the attacks of September 11, the GETS program has expanded more than six-fold within the financial sector. If you are interested in participating in this program, please contact your primary regulator. Each of the participating regulators serves as the administrative sponsor for the GETS program. If you are already a GETS user, please remember to test your cards on a quarterly basis.

A third important program that the Treasury created is the Protective Response Planning Program. This program brings together federal and local government officials, members of law enforcement and individuals from important financial institutions to develop and coordinate emergency responses to major disruptions at these specific institutions. Having personally participated in one such exercise for a very important institution, I can attest to its value. Watching the diverse array of law enforcement authorities - from the local police chief, to the county sheriff, the state police superintendent, the FBI, the United States Secret Service, and still others - coordinate their emergency response plans, in some cases for the first time, demonstrated how powerful a collaborative effort could be. The Protective Response Planning Program is open to the most critical financial institutions. If you are interested, please contact me.

Thank you for your time today. Thank you for attending this important conference.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 8, 2004
JS-1092

**Air Transportation Stabilization Board
Names Michael Kestenbaum As Executive Director**

The Air Transportation Stabilization Board (ATSB) has named Michael Kestenbaum as its Executive Director. Mr. Kestenbaum is replacing Brian C. Roseboro, Acting Under Secretary for Domestic Finance, Department of the Treasury, who has served as acting Executive Director of the ATSB since August 2003.

Mr. Kestenbaum was the first financial analyst hired by the ATSB after its creation. Prior to joining the ATSB, he was an analyst in the Investment Research Division at Goldman, Sachs & Co. in New York City, focusing on the airline industry. Mr. Kestenbaum is a graduate of Yale University.

The Chairman of the ATSB, Federal Reserve Board Governor Edward M. Gramlich, said "We are delighted that Michael Kestenbaum has agreed to take over as Executive Director. He has valuable private sector experience with the U.S. airline industry, as well as extensive institutional knowledge of the operations of the ATSB. He will play a vital role in helping the Board fulfill its responsibilities."

Additional information on the ATSB is available on its web site, www.treas.gov/atsb.

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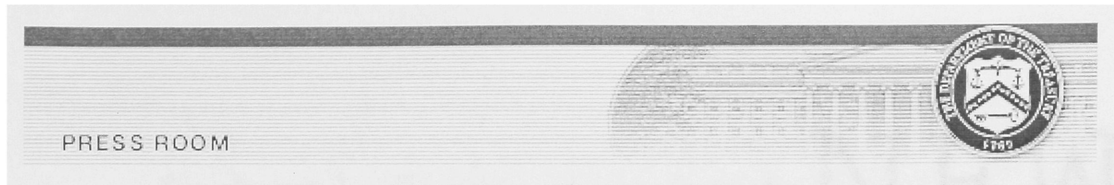

FROM THE OFFICE OF PUBLIC AFFAIRS

January 9, 2004
js-1093

Statement of Secretary John Snow on Employment Report

Following five months of job growth, the unemployment rate fell in December to a 14 month low. Regardless, today's report on December job growth demonstrates that while the fundamentals are in place, we must continue our efforts to strengthen the environment for job creation.

The fact is that while an index of manufacturing orders is at a fifty year high, construction spending is up, housing starts are at a twenty year high, retail sales are solid, and GDP growth is strong, the Administration will not be satisfied until every American who wants a job can get one.

We are on the right path to a strong recovery, and we must stay on the path.

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federal financing bank NEWS
WASHINGTON, D.C. 20220

FEDERAL FINANCING BANK

2004 PRESS RELEASE

January 2004

Brian Jackson, Chief Financial Officer, Federal Financing Bank (FFB) announced the following activity for the month of January 2004.

FFB holdings of obligations issued, sold or guaranteed by other Federal agencies totaled $31.3 billion on January 31, 2004, posting an increase of $451.7 million from the level on December 31, 2003. This net change was the result of increases in holdings of agency debt (U.S. Postal Service) of $282.3 million and in net holdings of government-guaranteed loans of $169.4 million. The FFB made 37 disbursements and received 11 prepayments during the month of January.

Below are tables presenting FFB January loan activity and FFB holdings as of January 31, 2004.

FEDERAL FINANCING BANK
January 2004 ACTIVITY

Borrower	*Date*	*Amount of Advance*	*Final Maturity*	*Interest Rate*	*Semi-Annually or Quarterly*

JS-1094

AGENCY DEBT					
U.S. POSTAL SERVICE					
U.S. Postal Service	1/02	$24,600,000.00	1/5/2004	1.000%	Semi-Annually
U.S. Postal Service	1/02	$206,600,000.00	1/6/2004	1.010%	Semi-Annually
U.S. Postal Service	1/30	$282,300,000.00	2/2/2004	0.969%	Semi-Annually
GOVERNMENT-GUARANTEED LOANS					
General Services Administration					
San Francisco Bldg Lease	1/30	$3,274,037.46	8/1/2005	1.722%	Semi-Annually
DEPARTMENT OF EDUCATION					
Shaw University	1/26	$9,698,445.90	10/1/2004	1.055%	Semi-Annually
RURAL UTILITIES SERVICE					
Arrowhead Electric #773	1/02	$500,000.00	12/31/2035	4.948%	Quarterly
Coastal Electric #2082	1/02	$3,000,000.00	12/31/2037	4.983%	Quarterly
Pickwick Electric Coop. #2074	1/02	$5,000,000.00	1/3/2033	4.895%	Quarterly
North Central Elec. #638	1/06	$884,000.00	1/2/2035	5.043%	Quarterly
Brazos Electric #844	1/07	$5,000,000.00	6/30/2004	1.019%	Quarterly
Brazos Electric #844	1/07	$5,000,000.00	6/30/2004	1.019%	Quarterly
Brazos Electric #844	1/07	$4,800,000.00	6/30/2004	1.019%	Quarterly
Eastern Maine Coop. #795	1/08	$815,000.00	12/31/2035	4.947%	Quarterly
Georgia Trans. Corp. #849	1/08	$71,559,811.00	12/31/2025	4.666%	Quarterly
New Horizon Elec. #791	1/12	$1,000,000.00	6/30/2004	0.959%	Quarterly
Satilla Electric #2083	1/13	$12,000,000.00	12/31/2037	4.862%	Quarterly
Southern Iowa Electric #2044	1/14	$500,000.00	12/31/2037	4.828%	Quarterly
Thumb Electric #767	1/14	$250,000.00	12/31/2035	4.791%	Quarterly
Volunteer Electric Coop. #803	1/14	$4,000,000.00	3/31/2011	3.464%	Quarterly
Clark Energy Coop. #2087	1/15	$2,500,000.00	6/30/2004	94.200%	Quarterly
Grundy Elec.Coop. #744	1/15	$500,000.00	6/30/2004	0.942%	Quarterly
Rutherford Electric #2091	1/15	$15,100,000.00	12/31/2037	4.782%	Quarterly
Blue Grass Energy #674	1/16	$5,000,000.00	6/30/2004	0.943%	Quarterly
Clark Electric Coop. #2043	1/16	$2,000,000.00	12/31/2037	4.753%	Quarterly
Webster Electric #703	1/16	$2,402,919.00	12/31/2014	3.430%	Quarterly
Charles Mix Elec. #630	1/20	$86,262.00	12/31/2030	4.633%	Quarterly
Carbon Power & Light #533	1/21	$371,232.00	7/1/2019	4.486%	Quarterly
Whetstone Valley #891	1/21	$617,000.00	12/31/2036	4.797%	Quarterly

Northern Electric Coop. #827	1/22	$1,600,000.00	6/30/2009	3.112%	Quarterly
Thumb Electric #767	1/22	$300,000.00	12/31/2035	4.761%	Quarterly
Tri-County Electric #876	1/22	$700,000.00	12/31/2036	4.777%	Quarterly
Missoula Elec. #688	1/23	$525,000.00	12/31/2029	4.563%	Quarterly
Northeast Texas Electric #2065	1/23	$42,264,000.00	1/3/2028	4.498%	Quarterly
St. Croix Elec Coop. #801	1/23	$500,000.00	12/31/2035	4.709%	Quarterly
Victory Electric #782	1/23	$500,000.00	12/31/2035	4.709%	Quarterly
Victory Electric #782	1/26	$500,000.00	12/31/2035	4.792%	Quarterly
Tri-State E.M.C. #730	1/27	$1,000,000.00	1/2/2035	4.834%	Quarterly

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FEDERAL FINANCING BANK HOLDINGS
January 2004
(in millions of dollars)

Program	***January 31, 2004***	***Dec. 31, 2003***	***Monthly Net Change 1/1/04- 1/31/04***	***Fiscal Year Net Change 10/1/03- 1/31/04***
Agency Debt:				
U.S. Postal Service	$2,532.30	$2,250.00	$282.30	($4,741.10)
Subtotal*	$2,532.30	$2,250.00	$282.30	($4,741.10)
Agency Assets:				
FmHA-RDIF	$680.00	$680.00	$80.00	($125.00)
FmHA-RHIF	$1,830.00	$1,830.00	$80.00	$80.00
Rural Utilities Service-CBO	$4,270.00	$4,270.20	$0.00	$0.00
Subtotal*	$6,780.20	$6,780.20	$0.00	($125.00)
Government-Guaranteed Lending:				
DOD-Foreign Military Sales	$1,622.70	$1,634.90	($12.20)	($65.70)
DoEd-HBCU+	$115.00	$105.00	$9.20	$35.70
DHUD-Comm. Dev. Block Grant	$1.00	$1.10	$0.10	($1.20)
DHUD-Public Housing Notes	$1,054.80	$1,054.80	$0.00	($78.50)
General Services Administration+	$2,143.60	$2,142.60	$1.10	($3.50)
DOI-Virgin Islands	$8.20	$9.60	($1.40)	($1.40)
DON-Ship Lease Financing	$597.30	$607.50	($10.20)	($10.20)
Rural Utilities Service	$16,334.60	$16,149.60	$185.10	$716.40

SBA-State/Local Devel Cos.	$69.80	$71.00	($2.10)	($7.60)
DOT-Section 511	$3.00	$3.00	$0.00	$0.00
Subtotal*	$21,950.10	$21,780.70	$169.40	$584.10
Grand total*	**$31,262.60**	**$30,810.90**	**$451.70**	**($4,282.00)**

figures may not total due to rounding; +does not include capitalized interest

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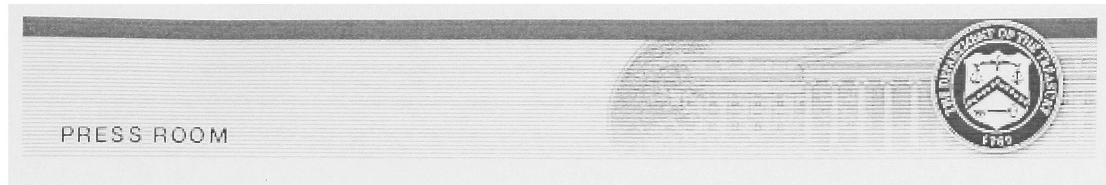
2003 Press Releases

Return to PRESS RELEASES

Last Updated on 2/19/04



FROM THE OFFICE OF PUBLIC AFFAIRS

January 13, 2004
js-1095

Media Advisory: Treasury Will Announce FY '05 Budget Proposals to Close Loopholes, Improve Compliance, and Simplify the Tax Code

Treasury Assistant Secretary for Tax Policy Pam Olson will hold a briefing on Tuesday, January 13, 2004 at 10:00 am in room 3327 (Large Conference Room). This briefing will provide information on new proposals that will be included in the President's FY '05 Budget to close loopholes, improve compliance, end several abusive tax avoidance transactions, and simplify the tax code.

Media without Treasury or White House press credentials planning to attend should contact Treasury's Office of Public Affairs at (202) 622-2960 with the following information: name, social security number and date of birth. This information may also be faxed to (202) 622-1999.

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PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 13, 2004
JS-1096

Treasury Announces New Budget Proposals
New Proposals Close Loopholes, Stop Abusive Tax Avoidance

Today the Treasury Department announced a series of legislative proposals included in the President's FY '05 Budget that are designed to close loopholes, halt several abusive tax avoidance transactions, and simplify the tax code. The President's FY '05 Budget reflects the Administration's continuing commitment to ensuring that all taxpayers pay their fair share of taxes, while reducing the needless cost borne by those attempting to comply. In addition, the President's FY '05 Budget provides for increases to the IRS' budget to enhance compliance.

Voluntary compliance with the tax laws is threatened when taxpayers use abusive transactions to avoid paying the taxes they owe. For the past three years, the Administration has acted aggressively to restore confidence in the tax system by halting the promotion of abusive transactions and bringing taxpayers back into compliance with the tax laws. The FY '05 budget proposals build on the Administration's prior proposals and on information gathered through IRS compliance programs. The new legislative proposals close loopholes and target identified abusive transactions and practices. As other abusive transactions are identified, the IRS will challenge the transactions in audits, and the Treasury Department and the IRS will work with Congress to enact any legislation necessary to address the transactions.

The President's FY '05 Budget includes $300 million for IRS efforts to ensure compliance with the tax laws, and increases the total IRS budget by 4.8%—significantly above the average for non-defense, non-homeland discretionary spending. The budget continues a three year trend of increasing resources for the IRS to improve compliance with the tax laws, particularly with respect to abusive tax avoidance transactions, while maintaining customer service to taxpayers.

Just as abusive tax avoidance transactions threaten voluntary compliance, so too does the complexity of the tax laws. Complexity imposes needless costs on honest taxpayers simply doing their best to comply with the law. Simplifying the tax laws makes it both less painful and less costly for Americans to fulfill their civic obligations. For these reasons, it is important to continue efforts to simplify the tax laws. The new FY '05 Budget proposals, all of which relate to the complexity borne by individuals and families, do not represent an exhaustive list. Rather, they serve as examples of the many steps that should be taken to make the tax code easier to understand and comply with. The Administration looks forward to working with Congress in further efforts to simplify the tax laws.

"The laws must ensure that those who would shirk their civic responsibilities cannot do so by exploiting unintended loopholes, and the IRS must ensure that taxpayers do not engage in abusive tax avoidance transactions," said Treasury Secretary John Snow. "These proposals would close loopholes and give the IRS the tools it needs to do the job. At the same time, we need to give honest Americans a better deal. We want to make it easier for those who pay their taxes, and harder for those who choose not to do so. While nobody likes paying taxes, we need to make it as simple and painless as possible. And reducing the burden of government on citizens and the economy remains a critical part of the President's six point plan for

"We are committed to restoring confidence in the tax system by ending the proliferation of abusive tax avoidance transactions and simplifying the tax code," said Treasury Assistant Secretary for Tax Policy Pam Olson. "Ultimately, there is no "silver bullet" or "one-size-fits-all" solution addressing abusive tax avoidance transactions—other than continuing to simplify the tax code and ensure that the tax results match the economic realities of the transactions. The proposals announced today make use of the information Treasury and IRS have gathered and build on actions and efforts already in progress to increase transparency."

"Among the areas for which we propose simplification are the education provisions. You shouldn't need a college degree to get help with your child's education, but the education provisions of the tax code are so complex that even tax advisors struggle to understand them. Our legislative proposals would greatly simplify the provisions and make it easier for everyone to get the help they need," Olson concluded.

"Curbing the use of abusive tax avoidance transactions by corporations and individuals is our top enforcement priority," said IRS Commissioner Mark W. Everson. "Stiffer penalties for failing to comply with the rules on the promotion of abusive transactions will get the attention of promoters, attorneys, accountants and other advisors."

IRS COMPLIANCE AND ENFORCEMENT PROPOSALS

Impose Penalties on the Failure to Disclose Potentially Abusive Transactions Penalties for nondisclosure by taxpayers and promoters are either nonexistent or insufficient. The Treasury Department's March 2002 legislative proposals would impose significant penalties on taxpayers who fail to disclose potentially abusive transactions on a return and on promoters who fail to comply with their registration and list-maintenance requirements.

Permit Uniform Disclosure Rules for Potentially Abusive Transactions - Disclosure works best when the IRS has multiple sources of information about a transaction. In that case, taxpayers and promoters will understand that their failure to disclose will eventually be discovered. Current statutory requirements do not permit completely uniform and consistent rules. The Treasury Department's March 2002 legislative proposals would change the promoter registration and list-maintenance provisions of the tax code to allow for uniform and consistent rules.

Permit Injunction Actions against Promoters who Repeatedly Disregard the Registration and List-Maintenance Requirements – Some promoters repeatedly disregard requirements in the tax code, including the registration and list-maintenance requirements. The Administration's proposal would confirm the Government's authority to enjoin the most egregious promoters of abusive tax avoidance transactions, as it is doing currently with promoters of tax scams directed primarily at individuals and small businesses.

Impose a Penalty for the Failure to Report an Interest in a Foreign Financial Account – Individual taxpayers are required to disclose on their tax returns interests in a foreign financial account, such as bank account. Under the Administration's proposal, a new civil penalty would be imposed on the failure to disclose foreign financial accounts, which often are used in tax avoidance transactions.

Curb Abusive Income-Separation Transactions – Some taxpayers continue to engage in transactions that separate the periodic income steam from an underlying income-producing asset in order to generate an immediate tax loss for one taxpayer and the conversion of current taxable income into deferred capital gain for another. Although the Tax code prohibits these transactions for bonds and preferred stock, taxpayers have been engaging in essentially identical transactions using similar assets, such as shares in a money-market mutual fund. Under the Administration's proposal, an income-separation transaction would be treated as a secured borrowing, not a separation of ownership. Debt characterization will ensure that the tax treatment of the transaction clearly reflects income.

Eliminate Obstacles to Disclosure - Some non-corporate taxpayers and practitioners have asserted the statutory tax practitioner privilege to avoid the disclosure of the identity of taxpayers who have entered into potentially abusive transactions. Delays in the disclosure of information about taxpayers who have entered into potentially abusive transactions also may prevent the IRS from examining these transactions before the statute of limitations expires. The Administration's proposal would expand the "corporate tax shelter" exception to the statutory tax practitioner privilege to all "tax shelters." The proposal also would confirm that the identity of any person that a promoter is required to identify is not privileged. In addition, the proposal would extend the statute of limitations for potentially abusive transactions that a taxpayer fails to disclose on a return until the transaction is disclosed to the IRS by either the taxpayer or the promoter.

Increase Penalties for False or Fraudulent Statements Made to Promote Abusive Tax Avoidance Transactions - Existing penalties are insufficient to deter promoters from making false or fraudulent statements regarding the claimed benefits of an abusive transaction. The Administration's proposal would significantly increase the penalty to up to 50 percent of the fees earned by the person making or furnishing the false statement in connection with the promotion of an abusive transaction.

Eliminate Abusive Transactions Involving Foreign Tax Credits Current law provides taxpayers with a credit for certain foreign taxes in order to eliminate the double taxation of foreign income (i.e., taxation by both the United States and the country where the income is earned). Taxpayers have structured transactions in an attempt to use foreign tax credits not to eliminate double taxation but inappropriately to reduce their U.S. tax liability on unrelated foreign income. The Treasury Department's March 2002 legislative proposals would deny foreign tax credits for foreign withholding taxes imposed on income if the underlying property generating the income was not held for a specified minimum period of time. In addition, the Administration's proposal would provide the Treasury Department with regulatory authority in order to prevent transactions that inappropriately separate foreign taxes from the related foreign income to take advantage of the foreign tax credit rules where there is no real risk of double taxation.
10-year revenue effect of all provisions above: $1.071 billion.

Stop Abusive Leasing Transactions with Tax-Indifferent Parties Taxpayers increasingly have used purported leasing transactions to "acquire" significant tax benefits from a tax-indifferent party, such as a municipal transit authority or foreign government, in exchange for a modest fee. These transactions do not involve any useful economic activity, such as the acquisition or financing of business assets, and instead simply move a tax benefit, including depreciation, from a party that cannot use it (the municipality or foreign government) to a party that can (the taxpayer). Congress sought to limit these transactions in 1984 but these rules have proved ineffective over time. The Administration's proposal would sharply limit the tax benefits claimed by the taxpayer in these transactions.
10-year revenue effect: $33.725 billion.

Require Charitable Deductions to Reflect Accurately the Value of the Donation The tax laws encourage donations to charities. Some taxpayers, however, recently have claimed deductions for contributions of patents, intellectual property, motor vehicles, and other property that far exceed the value of the property donated. The Administration's proposal would impose additional appraisal requirements and limit, in the case of patents and certain other intellectual property, the amount that can be deducted so that the charitable contribution deduction allowed matches the value of the donation.
10-year revenue effect: $4.771 billion.

Prevent Misuse of Tax-Exempt Casualty Insurance Companies The tax laws provide that certain small casualty insurance companies are not subject to federal income tax. The Treasury Department and the IRS are aware that some taxpayers have established insurance companies to claim tax-exempt status and improperly accumulate investment income tax-free. The Administration's proposal would prevent individuals from using this targeted exception to inappropriately earn investment income tax free.
10-year revenue effect: $1.184 billion.

Address the Tax Consequences of Changing Beneficiaries of a Section 529 College Savings Plan The Administration's proposal would resolve issues arising from the funding of section 529 college savings plans, changes to the beneficiaries or account owners of these plans, and distributions and withdrawals from these plans. Current law is unclear and these issues cannot be fully addressed through regulations. Until these issues are resolved, these ambiguities will permit taxpayers to avoid transfer taxes. The Administration's proposal makes the rules administrable and equitable and, therefore, would protect the fisc and further encourage savings for college expenses through these increasingly popular plans.
10-year revenue effect: $194 million.

Tighten the Deduction Limitation for Interest Paid to Related Parties - Current law denies a deduction for certain interest paid by a corporation to a related party to the extent the corporation's net interest expenses exceed 50 percent of its taxable income (computed with certain adjustments). This limitation only applies if the corporation's debt-equity ratio exceeds 1.5 to 1.0. Because of the opportunities available under current law to inappropriately reduce taxes on U.S. operations through the use of foreign related party debt, the Administration proposes to tighten the limitation for related party interest expense. The Administration proposal would eliminate the current law 1.5 to 1 debt-equity safe harbor and reduce the income threshold from 50 percent to 25 percent for related party interest. This proposal also would limit the carryforward period for disallowed interest and eliminate the carryover of limitation under current law so that taxpayers cannot use disallowed interest expense in another taxable year.
10-year revenue effect: $3.116 billion.

Prevent Avoidance of U.S. Tax on Foreign Earnings Invested in U.S. Property - Under current law, U.S. shareholders of a controlled foreign corporation must include in income their pro rata share of earnings of the corporation that are invested in certain U.S. property. Deposits with banks are excluded from the definition of U.S. property subject to this rule, however, so that taxpayers operating through foreign subsidiaries are not discouraged from using the U.S. banking system. This exception has been interpreted in a manner inconsistent with the underlying policy. For example, certificates of deposit have been issued by a U.S. affiliate in a transaction structured to take advantage of the bank exception. Under the Administration's proposal, the exception for deposits with persons carrying on the banking business would be modified to eliminate this potential for abuse.
10-year revenue effect: $234 million.

Modify Tax Rules for Individuals Who Give Up U.S. Citizenship or Green Card Status - If an individual gives up U.S. citizenship, or terminates long-term U.S. residency, with a principal purpose of avoiding U.S. tax, the individual is subject to an alternative tax regime for 10 years. The Administration proposes to improve compliance with the expatriation rules by: (1) replacing the subjective "principal purpose" test with an objective test, (2) providing that individuals who expatriate continue to be taxed as U.S. citizens or residents until they give notice of the expatriating act or termination of residency, (3) providing special rules for individuals who are physically present in the U.S. for more than 30 days per calendar year, (4) subjecting certain gifts of stock of closely-held foreign corporations by these individuals to U.S. gift tax, and (5) requiring annual reporting for these individuals.
10-year revenue effect: $273 million.

Curb Frivolous Returns and Submissions Penalties may apply to frivolous positions taken on a tax return. Penalties do not apply to other submissions, such as offers-in-compromise (OICs), offers to enter into installment agreements, and requests for collection due process hearings, that may be based on frivolous arguments and that may be filed for the purpose of delaying or impeding tax administration. The Administration's proposal would increase the penalty for frivolous returns and allow the penalty to be applied to frivolous submissions that are not withdrawn after IRS request. The IRS would be permitted to disregard non-return frivolous submissions that are not withdrawn.
10-year revenue effect: None.

Terminate Installment Agreements when Taxpayers Fail to File Returns or Make Tax Deposits The IRS cannot terminate an installment agreement even if a taxpayer fails to file required returns or fails to make required federal tax deposits. The Administration's proposal would permit the IRS to terminate an installment

agreement in these situations.
10-year revenue effect: None.

Streamline the Handling of Collection Due Process Cases The Tax Court and the U.S. district courts have jurisdiction over collection due process cases, and which court has jurisdiction over a particular case depends on the type of tax involved. The jurisdiction rules are unnecessarily complicated and have been used by some taxpayers to delay tax administration. The Administration's proposal would consolidate jurisdiction over collection due process cases in the Tax Court.
10-year revenue effect: None.

Improve Procedures for Taxpayers Seeking to Resolve Their Tax Liabilities - The Administration has two proposals to improve procedures for taxpayers seeking to resolve their tax liabilities. The Administration's first proposal would permit the IRS to enter into installment agreements that do not guarantee full payment of a liability over the life of the agreement. This will permit the IRS to work with a broader range of taxpayers who desire to resolve their tax liabilities. The Administration's second proposal would make counsel review of accepted offers-in-compromise more efficient without diminishing oversight over the offers that are accepted.
10-year revenue effect: $505 million.

Make the Payment of FMS Fees for Levies More Efficient The Financial Management Services (FMS) processes certain IRS levies. The Administration's proposal would permit FMS to retain a portion of the amount collected as its fee, thereby reducing Government transaction costs, while still crediting the taxpayer with the full amount collected. Revenue: No revenue effect.
10-year revenue effect: None.

Expand the Use of Electronic Filing - The IRS has taken a number of steps to expand the availability and increase the use of electronic filing, which reduces costs and speeds processing for both taxpayers and the Government. The Administration's proposal would extend the April 15 filing date to April 30 for returns that are filed electronically, provided that any tax due also is paid electronically. This proposal would encourage more taxpayers to file electronically and allow the IRS to process more returns and payments efficiently.
10-year revenue effect: None.

Permit Private Collection Agencies to Support the IRS' Collection Efforts - The IRS' resource and collection priorities do not permit the IRS to continually pursue all outstanding tax liabilities. Many taxpayers are aware of their outstanding tax liabilities but have failed to pay them, and the IRS cannot continuously pursue each taxpayer with an outstanding liability. The Administration's proposal would allow private collection agencies, or PCAs, to support the IRS' collection efforts in specific, limited ways. The proposal would enable Government to reach these taxpayers to obtain payment while allowing the IRS to focus its own enforcement resources on more complex cases and issues. PCAs would not have any enforcement power and would be carefully monitored to ensure that taxpayer rights are carefully protected.
10-year revenue effect: $1.531 billion.

SIMPLIFICATION PROPOSALS

Reduce Burden on Single Parents - Over 20 million single parents raising children are entitled to tax relief in the form of a more generous standard deduction and lower rates. But in order to qualify for the relief, single parents must satisfy the household maintenance test, a complicated set of rules that is difficult to understand and hard for the IRS to administer. The test also imposes a significant record-keeping burden on the single parent. The proposal would eliminate the household maintenance test and simply require that the taxpayers live with their child.

Simplify the Earned Income Tax Credit (EITC) To qualify for the EITC, taxpayers must satisfy requirements regarding filing status, the presence of children in their households, investment income, and their work and immigration status in

the United States. These rules are confusing, require significant record-keeping, and are costly to administer. The proposal would: (1) allow some estranged spouses who live with their children to claim the EITC if they live apart from their spouse for the last six months of the year; (2) allow certain taxpayers who live with children but do not qualify for the larger child-related EITC to claim the smaller EITC for very low-income childless workers; and (3) eliminate the investment income test for taxpayers who are otherwise EITC eligible. The proposal would also improve the administration of the EITC with respect to eligibility requirements for undocumented workers.

Consolidate and Simplify Higher Education Tax Benefits Taxpayers are faced with a range of options to reduce their taxes to pay or save for higher education. Taxpayers often have difficulty determining which alternative is best for them. In addition, the provisions are confusing and difficult to apply. The Administration proposes to simplify the choices students and parents face by consolidating the various provisions into two credits: the Hope credit and an expanded Lifetime Learning credit. The new Lifetime Learning credit would cover student interest (up to $2500) and would apply on a per-student rather than a per-taxpayer basis. The phase out limits for both credits would be raised, and the dollar limits would be indexed. The definitions of "qualified higher education expense" and "qualified higher education institution" would be made uniform throughout the Code. Other changes would be made to increase uniformity of definitions.

Make Computing the Child Tax Credit Easier - Taxpayers are required to satisfy income tests to determine the refundable child tax credit and the EITC. The requirements are different for the two credits. As a result, taxpayers must calculate their income twice. In addition, the credits have different US residency requirements. The additional child tax credit also requires families with three or more children to compute the amount of the credit twice to determine the higher amount. The proposal would use the same income and residency tests for the refundable child tax credit and the EITC. The proposal would also provide one computation to determine the credit amount.

Simplify the Taxation of Dependents The standard deduction for over 12 million dependents is determined by a complicated formula. The formula results in the filing of tax returns with very small amounts of tax liability. Additionally, special rules called the "kiddie tax" apply to investment income of young dependents. The "kiddie tax" requires complex calculations involving the parents' and siblings' income and tax rates. The proposal would simplify and expand the standard deduction for dependents. In addition, the proposal would tax young dependents based on their income alone and not on the income of their parents and siblings as well.

Simplify the Calculation of the Capital Gains Tax - Special tax rates apply to gains on certain types of assets like small business stock, real estate, and collectibles. These special rates complicate tax forms, worksheets, and instructions for all taxpayers with capital gains. The proposal would eliminate the various special rates for particular assets. Instead, fifty percent of the gain on these assets would be taxed at ordinary income tax rates and the remainder at the standard capital gains rate. In addition, special treatment for certain newly-issued small business stock would be eliminated.

Make Adoption Easier - The adoption tax credit and the exclusion for employer-provided adoption expenses (taxpayers may not use both provisions for the same expenses) are phased out for higher-income families resulting in unnecessary complexity. The proposal would eliminate the income phase-out for adoption tax benefits.

Ease Compliance Burden for Unemployment Insurance Household employers must separately pay Federal and state unemployment insurance taxes for their employees. This separate requirement is extremely burdensome. As a result, household employers and workers often fail to properly report those wages. The proposal would allow household employers to annually report and pay a combined federal and state unemployment tax to the federal government. Unemployment insurance benefits for household employees would continue to be paid by the state and reimbursed by the federal government.

Make Uniform Various Definitions of a Qualifying Child Families with children

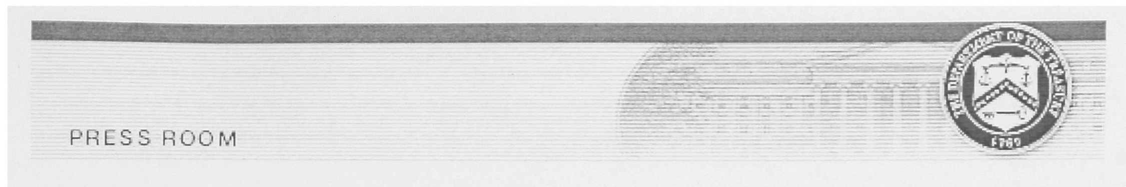
may be eligible for reduced taxes or for refundable credits through the dependent exemption, the head of household filing status, the child tax credit, the child and dependent care tax credit, and the earned income tax credit (EITC). Each of these tax benefits uses a definition of a qualifying child that is different in some way from the others. In addition, for some of these benefits, the taxpayer must provide over half the costs of supporting the child (the "support test"). Having different definitions of a qualifying child for different tax benefits is confusing for taxpayers and leads to errors. In addition, the support test, when it applies, is difficult to understand and requires taxpayers to keep extensive records. The proposal would make the definition of a qualifying child the same for each of the five child-related tax benefits. In addition, the support test would be eliminated. Instead, taxpayers would be required to live with the child for over half the year, which is a much simpler test to apply.
10-year revenue effect of all simplification provisions: -$5.756 billion.

ADDITIONAL IRS FY '05 BUDGET INFORMATION

Total IRS Funding – The President's FY 2005 Budget increases the total IRS budget by 4.8% to $10.674 billion.

Business Systems Modernization – The Presidents FY '05 Budget provides an installment of $285 million for the IRS to continue efforts to overhaul its antiquated computer system. Recent independent studies have shown that modernization needs to be resized to focus efforts on those programs which are proving to be successes.

-30-



FROM THE OFFICE OF PUBLIC AFFAIRS

January 15, 2004
JS-1097

Statement of Secretary John Snow on December Retail Sales

December's solid growth in the retail sector and upward revisions to November sales is consistent with a strengthening of the economy's underlying fundamentals. Along with healthy retail sales, last year ended with encouraging news in the form of record high homeownership rates, solid business investment, strengthening in the manufacturing sector, strong construction output and robust GDP growth. Unemployment claims – both initial claims and continuing claims – fell this week, indicating improvement in the labor market. We are on a path to sustained economic recovery.

However, looking forward, there is more to be done. Building on the boost provided by the Jobs and Growth Act, the President has proposed a six-point plan to further bolster economic growth. This Administration will continue its efforts until every American looking for work can find a job.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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January 16, 2004
JS-1098

Treasury International Capital Data for November 2003

Treasury International Capital (TIC) data for November are released today and posted on the U.S. Treasury web site (www.treas.gov/tic). The next release date, which will report on data for December, is scheduled for February 17, 2004.

According to the TIC data released today:

- Gross purchases by foreigners of U.S. long-term domestic securities from U.S. residents were $1,171 billion in November. Gross sales by foreigners of U.S. long-term domestic securities to U.S. residents were $1,089 billion in November.
  - Thus, *net* foreign purchases of U.S. long-term domestic securities from U.S. residents were $83 billion in November, which compares with $41 billion in October.
    - Net foreign purchases of U.S. Treasury notes and bonds from U.S. residents were $33 billion in November, which compares with $12 billion in October.
    - Net foreign purchases of U.S. agency bonds from U.S. residents were $11 billion in November, which compares with $9 billion in October.
    - Net foreign purchases of U.S. corporate bonds from U.S. residents were $30 billion in November, which compares with $21 billion in October.
    - Net foreign purchases of U.S. equities from U.S. residents were $9 billion in November, which compares with -$1 billion in October.
- Net purchases by foreign official institutions of U.S. long-term domestic securities in November were $21 billion, down from $23 billion in October. Net purchases by foreign official institutions of U.S. Treasury notes and bonds were $19 billion, which compares with $19 billion in October.
- Gross purchases by foreigners of long-term foreign securities from U.S residents were $321 billion in November. Gross sales by foreigners of long-term foreign securities to U.S. residents were $316 billion in November.
  - Thus, *net* foreign purchases of long-term foreign securities from U.S. residents were $5 billion in November, which compares with -$13 billion in October.

For the full November data set, including adjustments for repayments of principal on

asset-backed securities, as well as the historical series go to www.treas.gov/tic.

Related Documents:

- Treasury International Capital Table

Foreigners' Transactions in Long-Term Securities with U.S. Residents

	2001	2002	12 Months Through: Nov-02	Nov-03	Aug-03	Sep-03	Oct-03	Nov-03
Total Purchases, net	**501.2**	**574.6**	**571.0**	**670.2**	**49.9**	**4.3**	**27.8**	**87.6**
Total Gross Purchases	12,819.5	15,663.0	15,489.7	18,877.0	1,785.8	1,708.6	1,807.5	1,492.6
Total Gross Sales	12,318.3	15,088.4	14,918.7	18,206.7	1,735.8	1,704.4	1,779.7	1,405.0
Domestic Securities Purchased, net /1	**520.8**	**547.6**	**546.3**	**709.4**	**62.4**	**15.9**	**41.1**	**82.5**
Private, net /2	**494.1**	**506.1**	**511.5**	**575.8**	**62.4**	**4.3**	**18.3**	**61.6**
Treasury Bonds & Notes, net	15.7	111.0	111.9	151.8	26.1	-2.5	-7.4	14.6
Gov't Agency Bonds, net	146.6	166.7	160.9	137.5	8.5	-6.3	6.4	9.3
Corporate Bonds, net	217.6	176.1	176.3	258.9	16.5	19.3	20.3	28.8
Equities, net	114.2	52.2	62.5	27.6	11.4	-6.2	-1.0	8.9
Official, net	**26.7**	**41.5**	**34.8**	**133.6**	**0.0**	**11.5**	**22.9**	**20.9**
Treasury Bonds & Notes, net	2.8	8.9	3.4	105.0	-1.0	8.1	19.5	18.9
Gov't Agency Bonds, net	17.4	28.4	27.1	23.8	0.4	3.0	3.0	1.3
Corporate Bonds, net	4.3	6.2	6.5	5.0	0.4	0.5	0.7	0.9
Equities, net	2.2	-2.1	-2.2	-0.2	0.2	-0.1	-0.2	-0.2
Foreign Securities Purchased, net /3	**-19.6**	**27.0**	**24.7**	**-39.2**	**-12.5**	**-11.6**	**-13.3**	**5.1**
Foreign Bonds, net	30.5	28.5	32.5	20.7	1.0	-2.7	-5.1	-3.7
Foreign Equities, net	-50.1	-1.5	-7.8	-59.9	-13.6	-8.9	-8.2	8.8

/1 Foreign net purchases of of U.S. securities (+).
/2 Includes international and regional organizations.
/3 U.S. net acquisitions (-) of foreign securities.

Source: U.S. Department of the Treasury

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 16, 2004
JS-1099

MEDIA ADVISORY: Briefing On The Bush Administration's Budget Request For The Financial Crimes Enforcement Network

Treasury Deputy Assistant Secretary, Executive Office of Terrorist Financing and Financial Crime, Juan Zarate, and William Fox, Director of the Financial Crimes Enforcement Network (FinCEN) will brief reporters on Friday, January 16, 2004, at 12:00 pm EST in room 3327 at the main Treasury building. This briefing will provide information about the President's budget request for FinCEN and how it will assist in the administration's broader efforts in the effort to stop terrorist financing. This briefing will be on the record, but no cameras will be admitted -- this is a "pen and pad" briefing only.

Media without Treasury press credentials, including media with White House credentials, planning to attend should contact Frances Anderson in Treasury's Office of Public Affairs at (202) 528-9086 with the following information: name, social security number and date of birth by 11:00 am EST.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 16, 2004
JS-1100

Bush Administration Announces Budget Increase to help Fight Terrorist Financing and Financial Crime

The Bush Administration today announced that it will propose a 12.7% increase in the budget of the Financial Crimes Enforcement Network (FinCEN) to further strengthen our hand in the financial war on terror and other efforts against financial crime.

FinCEN, a bureau of the United States Treasury, plays a key role in the administration's broad effort to stop financial crimes and the flow of money to terrorist organizations. FinCEN works with the financial community to support local, state, and federal law enforcement and intelligence agencies to help prevent the abuse of our financial system by criminals and terrorists.

"*FinCEN is on the front lines every day, tracking down those who attempt to use the U.S. and global financial system to plot, fund, and perpetrate acts of terrorism around the world. By proposing to substantially increase FinCEN's resources, President Bush has reaffirmed the administration's commitment to aggressively fight terrorism on every front*," said Secretary of the Treasury John W. Snow.

Under President Bush's proposal, FinCEN will be able to continue acquiring and upgrading the technology and resources vital to its support of the nation's fight against terrorism and financial crimes.

"The men and women of FinCEN appreciate the administration's recognition of the key role we play in its efforts to stop financial crime and terrorist financing. The President's FY 2005 budget request will enable FinCEN to effectively enhance its ability to provide law enforcement and intelligence agencies with the types of strategic, financial information and analysis they need to investigate and bring criminals and terrorists to justice," said William J. Fox, Director of the Financial Crimes Enforcement Network.

The new resources that President Bush has proposed in his budget will be focused on three areas:

- Expand the capacity of FinCEN's Gateway program by at least 100%, increasing its user capacity from the current 1100 users to more than 2000 users. This program makes it possible for local, state and federal law enforcement officials to directly access information related to suspected money laundering activities. In addition the new resources will allow FinCEN to design and implement "BSA Direct" a new, state-of-the-art data retrieval system with advanced analytical tools and data mining capabilities. BSA Direct, which is currently under development, will provide a web-based, user-friendly tool to financial investigators.
- Increase by 25% the number of personnel dedicated to outreach to and regulatory support of industries that are covered by federal anti-money laundering programs for the first time. These efforts are an essential part of FinCEN's mission, which is, in part, to assist the financial services community in meeting its obligations to comply with regulations designed to help protect their institutions from being used as a conduit for the illegal proceeds of crime and terrorist financing.
- Increase the number of analysts to further strengthen FinCEN's ability to

provide strategic and tactical analytical products to law enforcement and the financial community which are essential in the effort to prevent money laundering and terrorist financing. These products range from trend and pattern information to investigative case support.

President Bush's budget request for FinCEN is only part of the administration's broader war on terrorist financing and other financial crimes. The President's budget also seeks a 3.6% increase for Treasury's Office of Foreign Assets Control (OFAC), which is responsible for identifying and blocking the assets of terrorists and terrorist sponsors..

Stopping and tracing tainted money flows depends upon transparent and accountable financial systems. Working together with other elements of the US government and the international community, the US Treasury Department has led the development of increased transparency and accountability in formal and informal financial systems around the world, making it more difficult and costly for terrorists and other criminals to raise, move and use funds in support of their operations. While the deterrent, preventive and investigative value of these efforts cannot be captured by statistics, the following developments indicate substantial progress in prosecuting the financial war on terror:

Since September 11, 2001:

- 1447 accounts, containing more than $139.1 million in assets, frozen worldwide including $36.7 million in the U.S.
- $64 million in additional terrorist related assets seized by authorities globally.
- 345 individuals and organizations listed as Specially Designated Global Terrorists (SDGTs) under Executive Order 13224.
- Countless millions in additional funds prevented from flowing to terrorists by disruption of terrorist financing networks, deterrence of donors, and international efforts to secure the world financial system from the financing of terror.

Several major sources of terrorist financing dismantled:

- In December, the U.S. and Saudi Arabian governments took joint action against a previously designated entity that was trying to reestablish itself under a new identity.
- In August, 2003, Sec. Snow announced the U.S. designation of several charities funding Hamas and several members of Hamas' senior leadership. In the weeks since, the European Union has now designated the political wing of Hamas.
- In support of previous action by European partners, the U.S. designated the Al-Aqsa International Foundation, a major source of funding to Hamas in April of 2003, helping to shut-down the German based charity.
- Fifty countries joined the U.S. to designate al-Qaida's primary partner in Southeast Asia, Jemaah Islamiyah, at the UN in 2002. In early 2003, two of the organization's leaders were subsequently designated at the UN, and Secretary Snow announced the designation of 20 more key members of JI at the APEC Ministerial Finance meeting in Thailand in September 2003.
- The Somali based al-Barakaat network once provided funding and transferred money to and from al-Qaida. The U.S. and our international partners took action to designate al-Barakaat and close down their operations in November of 2001.
- Three major U.S. based charities providing financing to terrorists, the Global Relief Foundation, Benevolence International Foundation and Holy Land Foundation for Relief and Development were designated and shuttered in December of 2001.
- Over 200 countries and jurisdictions have expressed their support in the financial war on terror.
- 173 countries have issued blocking orders freezing terrorist assets.
- More than 100 countries have passed new laws, strengthening their safeguards against terrorist financing.
- 84 countries have established Financial Intelligence Units to share

information on terrorist financing.
- The UN Security Council has approved Resolutions 1373 and 1455 that compel action by member states to combat terrorist financing.
- The Financial Action Task Force (FATF) has issued 8 Special Recommendations on Terrorist Financing and revisions to the 40 Recommendations on Money Laundering, providing international standards to prevent terrorist financing.

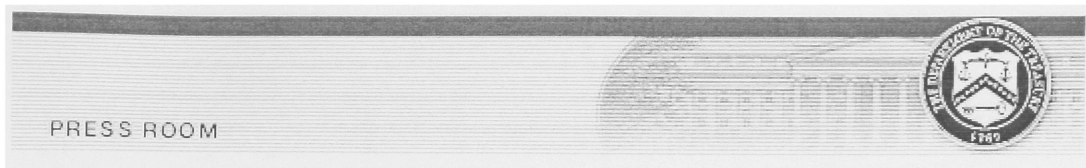
FinCEN Accomplishments since September 11, 2001:

- Law Enforcement Support: Since 9-11, FinCEN has supported 12,914 cases involving 82,832 subjects. Of these cases, 2,692, involving 20,240 subjects were related to terrorism.
- 314(a) Information Sharing: FinCEN's 314(a) program enables federal law enforcement agencies, through FinCEN, to reach out to over 29,000 financial institutions to locate accounts and transactions of persons that may be involved in terrorism or money laundering. Regulations require that law enforcement provide written certification that subjects submitted to FinCEN are reasonably suspected based on credible evidence of engaging in terrorist activity or money laundering.
- The system has processed 200 requests submitted by ten federal agencies from February 18, 2003 to December 31, 2003.
- These federal law enforcement organizations have submitted cases in the conduct of 68 terrorism/terrorist financing cases and 132 money laundering cases.
- There were 1,302 subjects certified by law enforcement and forwarded by FinCEN to financial institutions through the 314(a) system.

The feedback from law enforcement has been overwhelmingly positive and has resulted in the discovery of hundreds of suspect accounts and transactions in addition to the issuance of the following:

- 472 Grand Jury Subpoenas
- 11 Search Warrants
- 21 Administrative Subpoenas/Summons
- 3 Indictments
- **FIU Support**: FinCEN also supports U.S. law enforcement through the 84 Financial Intelligence Units (FIUs) throughout the world. Since 911, FinCEN has referred 598 requests on behalf of US law enforcement of which 346 related to terrorism.
- **Hotline:** FinCEN's financial institutions hotline, an initiative created by FinCEN immediately following the events of September 11th, allows the financial community to immediately alert law enforcement on suspected terrorist financing or money laundering activities. To date, there have been 789 Hotline Tips that have been referred to law enforcement.
- **Regulatory Efforts**: 22 final, proposed and/or advance notices of proposed rulemaking were issued under the Patriot Act to strengthen anti-money laundering and terrorist financing efforts.

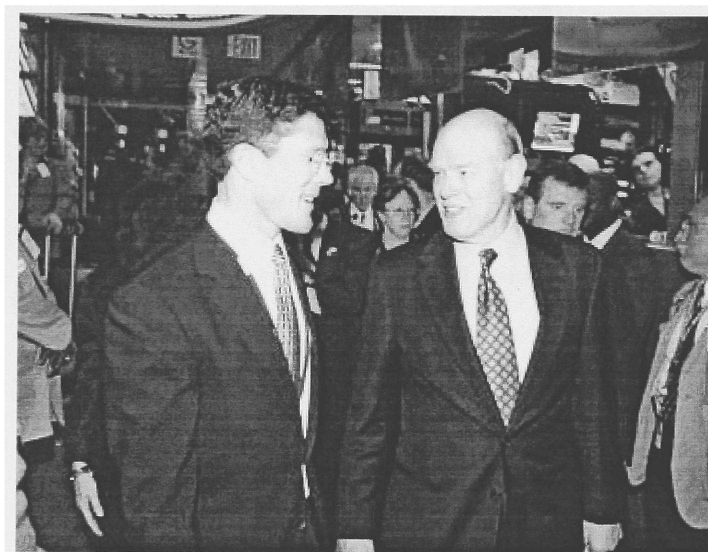
FinCEN submitted its Report to Congress on Informal Value Transfer Systems (IVTS) as mandated by Section 359 of the USA PATRIOT Act.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 16, 2004
JS-1101

Secretary John Snow on Friday toured the trading floor of the New York Stock Exchange with NYSE CEO John Thain. (NYSE photo)



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Only call this number if you are a member of the media.

High Resolution Image

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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January 16, 2004
js-1102

U.S. Designates Bin Laden's Mouthpiece

WASHINGTON -- The U.S. Treasury Department today announced the designation of the man who stood beside Usama bin Laden when he declared responsibility for the attacks of September 11th. Today's action comes in response to the designation of this individual as a terrorist by the United Nations.

Sulaiman Jassem Sulaiman Abo Ghaith (Abo Ghaith) became the spokesperson for al-Qaeda after the attacks of September 11th, 2001. He repeatedly appeared in broadcasts on behalf of al-Qaeda, claiming responsibility for that attack and others, including the November 2002 suicide attacks in Kenya that killed 13 people. Although he was born in Kuwait, the Kuwaiti government revoked his citizenship in 2001.

Today's action is taken under obligations to freeze the assets of individuals and organizations listed by the UN. The name was originally submitted to the UN by another country for listing. A UN listing requires all Member States to freeze the assets of those listed and to bar cross-border travel. The UN listed this individual on Friday, January 16th.

With today's action, the U.S. and our international partners have designated 346 individuals and organizations as terrorists and terrorist supporters and have frozen over $139.1 million in terrorist assets.

More information regarding Abo Ghaith is attached.

-30-

Related Documents:

- Sulaiman Jassem Sulaiman Abo Ghaith (Abo Ghaith)

Sulaiman Jassem Sulaiman Abo Ghaith

AKAs: Abo Ghaith; Sulaiman abu Ghaith

DOB: December 14, 1965

POB: Kuwait

Sulaiman Jassem Sulaiman Abo Ghaith ("Abo Ghaith") has been the official spokesman of al-Qaeda since his appointment to that position after the attacks of September 11, 2001. Shortly after these attacks, he appeared seated beside Usama bin Laden (UBL) and Ayman Zawahiri in a video that aired October 9th on al Jazeera, after the start of U.S. Operation ENDURING FREEDOM in Afghanistan. He has also appeared alone as the mouthpiece of bin Laden, praising the attacks of September 11th and threatening more. (The text of his statement, broadcast on October 9, 2001, can be found at http://news.bbc.co.uk/low/english/world/middle_east/newsid_1590000/1590350.stm.) In December of 2002, he broadcast a message claiming al-Qaeda's responsibility for the November 2002 suicide attacks in Kenya that killed 13 people and called on al-Qaeda fighters to "prepare themselves seriously for the next phase which will be bigger and more serious."

Although he was born in Kuwait, the Kuwaiti Government announced in October 2001 that Abo Ghaith's citizenship was revoked in its "national interest."

Abo Ghaith was a high school teacher and preacher at a mosque in Kuwait. He fought in Afghanistan, accused the U.S. government of killing children in Iraq through UN sanctions, and joined Muslim guerillas fighting in Bosnia-Herzegovina in the summer of 1994. In the late 1990s, the government banned him from the mosque where he was preaching because he strayed from officially approved religious themes, making strident and frequent attacks against the Kuwaiti government and other Arab governments. After being banned from the mosque, Abo Ghaith taught high school religion classes. Several individuals arrested for their involvement in al-Qaeda have stated they were recruited into the organization by Abo Ghaith. Indeed, while he lived in Kuwait before September 11, 2001, his mission was to recruit elements for training in bin Laden's camps in Afghanistan. At the end of the school year in 2001, he made at least two trips to Afghanistan.

Press reports indicate that Abo Ghaith is in custody in Iran.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 20, 2004
JS-1103

Remarks to the Brazil-U.S. Business Council
John B. Taylor
Under Secretary of the Treasury for International Affairs
2004 Strategic Planning Meeting Luncheon
U.S. Chamber of Commerce, Washington, D.C.

I would like to thank the Council for inviting me here today. It's my pleasure to provide comments to this distinguished group alongside Assistant USTR Chris Padilla and Otaviano Canuto, whom I'm happy to welcome to Washington as Brazil's new Executive Director at the World Bank.

The overriding objectives of U.S. economic policy—whether domestic or international—are maintaining macroeconomic stability and increasing economic growth. It is useful to think about what has happened in Brazil over the last year and what the priorities are for the upcoming year in this context.

Improving Macroeconomic Stability: President Lula's First Year in Office

When I spoke at this event last year, President Lula had been in office less than one month. While early indications were very positive, many Brazil observers and Brazilians themselves were still uncertain regarding the direction of a Lula presidency, especially with regard to economic policy. I noted at the time that we in the U.S. Treasury were encouraged by President Lula's balanced economic agenda— anchored in the maintenance of macroeconomic stability and driven by a focus on economic growth to achieve the social objectives laid out by President Lula in his inaugural address. Today, more than one full year President Lula's term, I'm pleased to report that our optimism was well-placed.

President Lula and his Administration were quick to implement disciplined economic policies aimed at achieving economic stability. The components of Brazil's economic agenda are well-known to this audience, but I think they merit review because it is easy to forget just how far we have come over the last year. Sound policy choices—and strong Brazilian ownership of these policies—have been the decisive factor in restoring financial market confidence in Brazil.

To begin, President Lula sought to control spending by committing Brazil to a primary surplus aimed at achieving sustainability of Brazil's public debt. Brazil over-performed on its IMF primary surplus target throughout 2003. President Lula made good on his promise to reform the public pension system and to reduce the deficit stemming from public pension payments. Reducing poorly-targeted spending in areas like pensions helps the government protect spending for priority areas such as sanitation and key social initiatives such as Bolsa Familia. The Administration has also started down the road to much-needed tax reform, it successfully passed tax measures necessary to ensure Brazil's fiscal sustainability in the near and medium-term. There is recognition that important reforms to correct inefficiencies in Brazil's tax code must be addressed in the context of fiscal stability. This is a fiscal reform record that demonstrates the Lula Administration's ability to build consensus on tough issues. We know it will need to sustain this consensus as it pursues other elements of the growth agenda.

In the area of monetary policy, the Central Bank demonstrated its commitment to

the inflation-targeting regime and withstood significant pressures to prematurely relax monetary policy. This policy has resulted in a steady reduction of inflation expectations in 2003, which peaked at 12.6 percent in March 2003. Statistics released last week show that consumer inflation for 2003 was 9.3 percent. Expectations for 2004 have followed a similar declining trend and currently stand at less than 6 percent, close to the Central Bank's target of 5.5 percent. Locking-in a lower inflationary path will be amply rewarded in the form of lower borrowing rates and higher economic growth. Granting the Central Bank formal autonomy will be an important next step to increase transparency and further reinforce expectations of low inflation.

Brazil also took tangible steps to reduce vulnerabilities to future shocks. One example is Brazil's concerted effort to accumulate international reserves in a manner consistent with Brazil's floating exchange rate and inflation-targeting monetary policy. Net international reserves—that is reserves excluding IMF disbursements—increased from $14 billion at end-2002 to $17 at end-2003, while the real appreciated 15 percent over the course of the year.

Another example is the government's strategy to aggressively reduce its reliance on foreign currency-linked debt. In one year, the Treasury reduced the amount of foreign currency-linked debt as a percent of Brazil's internal public debt outstanding from 22.4 percent at the end of 2002 to 10.8 percent at the end of 2003. This result exceeds the government's most optimistic target for reducing Brazil's direct fiscal exposure to currency swings. Finally, the government is making a concerted effort to deepen domestic financial markets by introducing the direct auction of public securities through the internet, which should both diversify Brazil's sources of funding and help increase potential sources of funds for the private sector.

Markets have reacted to this concerted progress. After approaching nearly 4.0 to the dollar in October 2002, the real rebounded strongly in 2003 and has been relatively stable in a range of 2.8 to 3.0 to the dollar since last April. Let us not forget that Brazil's sovereign risk spread soared to 2,400 basis points over U.S. Treasuries during the fall of 2002. Today, that sovereign risk spread stands at about 400 basis points. Just last week Brazil issued its first global bond of 2004—a $1.5 billion, 30-year bond that priced at just 376 basis points over the benchmark U.S. Treasury. Brazil has now completed $3 billion in external placements out of a planned $5.5 billion for 2004, having pre-financed $1.5 billion at the end of 2003. Beyond the government, the lower sovereign spread has positive implications for Brazilian companies, who can and have returned to international markets to raise capital in 2003 and 2004.

The official community has also signaled its confidence. Brazil has entered a new phase in its relations with the IMF. Late last year, Brazil and the IMF extended the program on a precautionary basis through early 2005. The program extension is designed as an exit strategy to unwind Brazil's obligations to the IMF in a way that won't undermine Brazil's reserve position or damage market confidence. It is clear that Brazil is moving away from reliance on official finance and has taken control of its own reform strategy. The United States supported this exit strategy as it has supported Brazil's consistently strong performance in meeting IMF commitments.

Increasing Economic Growth: The Agenda Ahead

Having achieved such substantial progress in restoring economic stability, it is natural that the focus in Brazil should now turn to increasing economic growth. This means addressing some of the key microeconomic impediments to higher rates of economic growth.

One priority is reducing the cost of credit and expanding access to capital. According to a recent World Bank report on Brazil, less than 20 percent of small enterprises have access to outside sources of financing. Nearly one-third of entrepreneurs cite the lack of credit as a major obstacle to business growth. The Brazilian government's 2004 agenda includes a number of measures designed to reduce the cost and expand the availability of credit, including: the passage and implementation of pending bankruptcy reform; implementation of measures to allow workers to pledge a portion of their wages as loan collateral; and giving borrowers

and lenders access to a centralized credit rating system in order to encourage competition in the banking sector.

Deregulation also has to be a priority. Entrepreneurship is encouraged by eliminating unnecessary administrative procedures. In Brazil, the cumbersome process of starting a business, which includes separate licensing and tax registration at various levels within the government, serves as a disincentive to business creation. The government has indicated its plans to examine measures to simplify and reduce registration requirements for business and address overlaps and redundancies between different agencies and levels of government.

A clear and transparent regulatory environment is critical to attracting new investment in key industries such as energy and telecommunications. The government recently unveiled plans to boost investment in key infrastructure projects through Public Private Partnerships.

Eliminating distortions in labor markets and bringing more workers into the formal labor market will also encourage investment as well as create jobs. Today, millions of workers in Latin America are forced into the informal labor sector, as employers find hiring employees through formal channels prohibitively expensive. By one estimate, more than half of the Brazilian labor force is employed in the informal sector. Addressing this problem requires action to address disincentives, such as high payroll taxes, that discourage job creation in the formal sector.

Changes to put in a place a simpler, more efficient tax system are also essential for getting incentives right for production and investment. The Lula Administration has committed to pursuing tax reform designed to make the tax system simpler, more efficient and socially just. Conversion of the cascading turnover tax, which disadvantages certain activities with long production chains, into a value-added tax is one example of this.

U.S.-Brazil Engagement

Raising economic growth is critical to combating poverty, promoting social development, and strengthening democracies throughout the Western Hemisphere. This was an important theme that emerged from last week's Special Summit of the Americas in Monterrey, which provided a broad endorsement of the kinds of sound economic policies needed to bolster economic growth across the Hemisphere. The Summit also provided the opportunity to launch specific initiatives to address the microeconomic impediments to higher growth. The United States proposed specific initiatives to triple IDB-catalyzed credit to small businesses, reduce the time required to start a business, and halve the cost of sending remittances from migrant workers to their families.

The U.S.-Brazil Group for Growth was inaugurated last year following the meeting between President Bush and President Lula. It provides a venue for advancing discussions on ways to increase economic growth in Brazil and the United States. We view it as a new model for engaging on economic policy in this region. We meet as two, large, sophisticated economies with much to teach each other on accelerating growth and reducing poverty. The inaugural meeting of the Group in August provided an opportunity to examine and compare the how productivity is measured in Brazil and the United States, and how such measurements are used in the conduct of economic policy. We also considered the relationship between investment and productivity growth over long periods of time in both countries. We plan to build on this discussion at the next meeting of the Group due to be held in Brazil in the first quarter of this year. This and future meetings will take up concrete policies for encouraging entrepreneurship, job creation and investment.

Again, I thank the Council for inviting me to speak with you today and I welcome your views on the outlook for Brazil and the kinds of issues we should focus on in the Group for Growth.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 21, 2004
JS-1104

**Media Advisory:
Treasury, OMB and IRS to Launch Second Annual
free file Initiative on Thursday**

The Department of Treasury, Office of Management and Budget and Internal Revenue Service will launch the second year of the IRS Free File initiative during a news conference at 1:15 p.m. Thursday, January 22. This initiative allows the majority of Americans to prepare and file taxes online electronically for free.

Treasury Secretary John W. Snow, OMB Director Joshua B. Bolten, IRS Commissioner Mark W. Everson, and Mike Cavanagh, the Executive Director of the Free File Alliance, will re-launch the Free File initiative and give brief remarks. Terry Lutes, IRS Associate Chief, Information Technology Services, will provide a demonstration of the Free File web site and will brief reporters. The Free File program is the product of a public-private sector pact between the IRS and Free File Alliance, LLC, a consortium of tax software companies.

The event will be featured in a live Webcast available through www.ustreas.gov .

The news conference will be held at the Treasury Department's press room (Room 4121). The room will be available for camera set up beginning at noon.

Media without Treasury press credentials should contact Treasury's Office of Public Affairs at (202) 622-2960 with the following information: name, Social Security number and date of birth. This information may also be faxed to (202) 622-1999.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1106

MEDIA ADVISORY
Department of the Treasury to Announce Joint Action with Saudi Arabia in the Financial War on Terror

Treasury Secretary John Snow today will announce a joint United States action with Saudi Arabia in the financial war on terror. The announcement will be followed by a briefing by officials from the Department of the Treasury, Department of State and the Saudi Arabian government. Today's joint action with Saudi Arabia is another important step in our ongoing war against terrorism and terrorist financing. The briefing will be an on the record, on camera briefing.

WHAT: Announcement and Briefing

WHEN: 11:00 AM EST

WHERE: Department of the Treasury, Room 4121

WHO: Statement by Secretary John W. Snow, followed by statements and Q & A with:

Juan Zarate, Deputy Assistant Secretary for Terrorist Financing and Financial Crime,
Department of the Treasury
Ambassador J. Cofer Black, Coordinator for Counterterrorism,
Department of State
Tony Wayne, Assistant Secretary Bureau of Economic and Business Affairs,
Department of State
Adel Al-Jubeir, Foreign Policy Advisor to Saudi Crown Prince Abdullah

Today's announcement and briefing will be webcast live at www.treasury.gov

Media without Treasury press credentials planning to attend today's event should contact the Treasury Public Affairs office at 202/622-2960 with the following information: name, social security number and date of birth. Media with White House press credentials must call to be cleared in to the Treasury Building.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1107

Prepared Remarks of Treasury Secretary John Snow to Announce Joint U.S. and Saudi Action Against Four Branches of Al-Haramain in the Financial War on Terror

Thank you very much for being here today.

I am very pleased to announce that the United States and Saudi Arabia have joined together today to take action against four branches of the Al-Haramain organization. Today's designation is another important victory in our ongoing war against the spread of terrorism and terrorist financiers and another demonstration of our partnership in the war against terror.

The four branches of Al-Haramain that we are singling out today have not only supported the plotting of despicable acts of terror, but they have done so by exploiting countless individuals who believed that by supporting Al-Haramain, they were, in fact spreading good will to many in need of a helping hand.

The four branches of Al-Haramain have cloaked themselves in the virtue of charity, only to fund and support terrorist organizations around the world such as the al-Qaeda network.

These four branches located in Indonesia, Kenya, Tanzania, and Pakistan have ignored past orders to cease their operations.

By designating these organizations under the President's Executive Order Number 13224, and joining with Saudi Arabia to call on the United Nations 1267 Sanctions Committee to designate these groups as well, we bring to bear the full weight of the international community.

We will continue to vigilantly work to ensure that these groups will no longer be able to disguise themselves as legitimate and benevolent organizations in order to undermine peace and freedom.

We know generous givers to charities provide hundreds of millions of dollars to improve the lives of countless people around the world.

We will not interfere with the noble work of legitimate charities.

But donors need to be assured that their contributions are being used for their intended purposes -- and not to fuel the activity of terrorists.

Make no mistake; this administration will continue to take aggressive actions, both domestically and internationally, to ensure that charities are not being abused by terrorists or other criminals.

Just days ago, during the State of the Union address, President Bush stated that our greatest responsibility is the active defense of the American people. Twenty-eight months have passed since September 11th, 2001 -- over two years without an attack on American soil. As the President said, it is tempting to believe

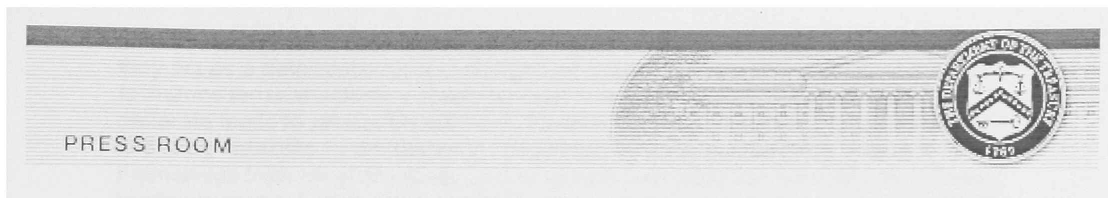
that the danger is behind us. But the terrorists continue to plot against America and the civilized world.

However, we too are on the offensive against the terrorists who started this war. We're tracking al Qaeda around the world, and nearly two-thirds of their known leaders have now been captured or killed.

As part of the Administration's offensive against terror the President mentioned during his national address, the Treasury Department is confronting networks that funnel money to terrorists.

The United States, Saudi Arabia, and our other partners around the globe have spoken out loud and clear – terrorism has no place in a civilized world. We will continue to work with Saudi Arabia and all our allies in the war against terror to seek out those who bankroll terrorist organizations and shut them down.

Thank you very much.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1108

Treasury Announces Joint Action with Saudi Arabia Against Four Branches of Al-Haramain In The Fight Against Terrorist Financing

Once again, the United States and Saudi Arabian governments are joining together to ask the United Nations' 1267 Sanctions Committee to add four branches of the Al-Haramain Islamic Foundation to its consolidated list of terrorists tied to al-Qaida, Usama bin Laden and the Taliban. Today's designation of the Al-Haramain branches in Indonesia, Kenya, Tanzania, and Pakistan under Executive Order 13224 is the latest in a series of public joint actions with our ally in the war on terrorist financing. These branches have provided financial, material and logistical support to the al-Qaida network and other terrorist organizations.

"The United States and Saudi Arabia share a deep commitment to fighting the spread of terrorism in all its forms. The branches of al Haramain that we have singled out today not only assist in the pursuit of death and destruction; they deceive countless people around the world who believe that they have helped spread good will and good works. By working together to take action today and calling on the United Nations to do the same, our two countries send a clear message: those who hide intensions of terror behind a veil of benevolence and charity will not escape justice from the international community," said Secretary John W. Snow.

The Saudi government in 2003 ordered Al-Haramain to close all of its overseas branches. Al-Haramain stated it closed branches in Indonesia, Kenya, Tanzania, and Pakistan, but continued monitoring by the United States and Saudi Arabia indicates that these offices and or former officials associated with these branches are either continuing to operate or have other plans to avoid these measures. The actions by the Bosnia-Herzegovina branch, designated in March 2002, to reconstitute itself and continue operations under the name, "Vazir," is one example. Similarly, the Indonesian branch of Al-Haramain has attempted to operate under an aka.

The four branches being designated today are only the most recent of Al-Haramain's overseas branches to be investigated, and the U.S. remains committed to ensuring that the branches of this charity can not be used to support terrorism. The Saudi Arabian government has informed the host countries that these entities are not Saudi entities and should be treated appropriately under local law. Designation at the UN triggers international obligations on all member countries, requiring them to take steps to ensure that these offices can not continue to use their remaining infrastructure or finances to fund or otherwise support terrorism. It is also a critical action to publicly identify these supporters of terrorism, providing warning to other entities that they are prohibited from doing business with them.

The Treasury Department is committed to stopping terrorism by taking action against those who fund it. With this designation, 350 individuals and entities will have been designated under President Bush's Executive Order aimed at freezing the assets of terrorists and their supporters – Executive Order 13224. At least $139 million in assets has been kept out of the control of terrorists as a result of efforts by the United States and its allies.

Blocking actions are critical to combating the financing of terrorism. When an action is put into place, any assets that assets exist in the formal financial system at the

time the orders are frozen. Blocking actions serve additional functions as well, e.g., they act as a deterrence for non-designated parties who might otherwise be willing to finance terrorist activity; expose terrorist financing "money trails" that may generate leads to previously unknown terrorist cells and financiers; disrupt terrorist financing networks by encouraging designated terrorist supporters to disassociate themselves from terrorist activity and renounce their affiliation with terrorist groups; terminate terrorist cash flows by shutting down the pipelines used to move terrorist-related assets; force terrorist to use alternative, more costly, and higher-risk means of financing their activities; and engender international cooperation and compliance with obligations under UN Security Council Resolutions.

The United States works to preserve the sanctity of charitable giving and the value of humanitarian aid provided by charities of all faiths. In this context, we are working to identify those charities that are abusing the trust of their donors. In addition to today's designation's over 10 charities have been designated by the United States because of their support to terrorism, including

- The Holy Land Foundation for Relief and Development (based in U.S.) (December 2001)
- Two Al-Haramain Branches (Bosnia-Herzegovina/Somalia) (March 2002)
- Global Relief Foundation (U.S.) (October 2002)
- Benevolence International Foundation (U.S.) (January 2003)
- Al Aqsa Foundation (Germany/Europe) (May 2003)
- Commite de Bienfaisance et de Secours aux Palestiniens (France) (August 2003)
- Association de Secours Palestinien (Switzerland) August 2003)
- Interpal (United Kingdom) (August 2003)
- Palestinien Association in Austria (Austria) (August 2003)
- Sanibil Association for Relief and Development (Lebanon)
- Al Akhtar Trust (Pakistan) (October 2003) (Al Akhtar was assuming a role that had been held by the Al Rasheed Trust, another Pakistan-based charity that was designated as part of the annex to E.O. 13224).

Like the United States, the Saudis have been victims of al-Qaida. They are an important partner in the war on terrorist financing, and have taken important and welcome steps to fight terrorist financing.

- The Saudis worked with the United States to establish a U.S.-Saudi task force in
- Riyadh focused on combating terrorist financing and establishing initiatives to better regulate charities.
- On March 11, 2002, the United States and Saudi Arabia enacted the first joint designation by blocking the funds of the Somalia and Bosnia-Herzegovina branches of Al-Haramain because these branches were diverting charitable funds to terrorism. When it became apparent that Al-Haramain was continuing to operate under a new name in Bosnia-Herzegovina, the United States and Saudi Arabia joined in asking the UN to add the a/k/a, "Vazir," to the consolidated list.
- In August of 2002, Saudi Arabia joined the U.S. in the designation of Wa'el Julaidan, a key terrorist financier who had known associations with Usama bin Laden and headed several non-governmental organizations that provided financial and logistical support to al-Qaida.
- Saudi Arabia also supported the addition of the Jeddah-based terrorist financier, Yasin Al-Qadi, to the UN's consolidated list in October 2001.

Basis for Designation

Information in the possession of the U.S. government indicates these offices have provided financial, material and logistical support to Usama bin Laden's (UBL's) al-Qaida network and other terrorist organizations. These branches are subject to designation under Executive Order 13224 pursuant to paragraphs (d) (i) and (d) (ii) based on a determination that they assist in, sponsor or provide financial, material, or technological support for, or financial or other services to or in support of, or are otherwise associated with, persons listed as subject to E.O. 13224. Because this support is being provided to Usama bin Laden, al-Qaida, and/or the Taliban, these

branches also meet the standard to be included on the United Nations' 1267Sanctions Committee's consolidated list. In addition to requiring UN Member States to freeze assets without delay, inclusion on this list triggers obligations to implement other sanctions, such as a travel ban and arms embargo.

AL-HARAMAIN FOUNDATION (INDONESIA)

- In 2002, money purportedly donated by AHF for humanitarian purposes to non-profit organizations in Indonesia was possibly diverted for weapons procurement, with the full knowledge of AHF in Indonesia.

- Using a variety of means, AHF has provided financial support to al-Qaida operatives in Indonesia and to Jemaah Islamiyah (JI). According to a senior al-Qaida official apprehended in Southeast Asia, Omar al-Faruq, AHF was one of the primary sources of funding for al-Qaida network activities in the region. The U.S. has designated JI, and the 1267 Committee has included it on its list, because of its ties to al-Qaida. JI has committed a series of terrorist attacks, including the bombing of a nightclub in Bali on October 12, 2002 that killed 202 and wounded over 300.

AL-HARAMAYN FOUNDATION (KENYA & TANZANIA)

- Information available to the US shows that AHF offices in Kenya and Tanzania provide support, or act for or on behalf of AIA and Al-Qaida. AIAI shares ideological, financial and training links with al-Qaida and financial links with several NGOs and companies, including AHF, which is used to transfer funds. AIAI also has invested in the "legitimate" business activities of AHF.

- As early as 1997, U.S. and other friendly authorities were informed that the Kenyan branch of AHF was involved in plotting terrorist attacks against Americans. As a result, a number of individuals connected to AHF in Kenya were arrested and later deported by Kenyan authorities.

- In August 1997, an AHF employee indicated that the planned attack against the U.S. Embassy in Nairobi would be a suicide bombing carried out by crashing a vehicle into the gate at the Embassy. A wealthy AHF official outside East Africa agreed to provide the necessary funds. Information available to the U.S. shows that AHF was used as a cover for another organization whose priorities include dislike for the U.S. Government's alleged anti-Muslim stance and purposed U.S. support for Christian movements fighting Islamic countries.

- Also in 1997, AHF senior activities in Nairobi decided to alter their (then) previous plans to bomb the U.S. Embassy in Nairobi and instead sought to attempt the assassination of U.S. citizens. During this time period, an AHF official indicated he had obtained five hand grenades and seven "bazookas' from a source in Somalia. According to information available to the U.S., these weapons were to be used in a possible assassination attempt against a U.S. official.

- Information available to the U.S. shows that a former Tanzanian AHF Director was believed to be associated with UBL and was responsible for making preparations for the advance party that planned the August 7, 1998, bombings of the U.S. Embassies in Dar Es Salaam, Tanzania, and Nairobi, Kenya. As a result of these attacks, 224 people were killed.

- Shortly before the dual-Embassy bombing attacks in Kenya and Tanzania, a former AHF official in Tanzania met with another conspirator to the attacks and cautioned the individual against disclosing knowledge of preparations for the attacks. Around the same time, four individuals led by an AHF official were arrested in Europe. At that time, they admitted maintaining close ties with EIJ and Gamma Islamiyah.

- Wadih el-Hage, a leader of the East African al-Qaida cell and personal secretary to UBL, visited the Kenya offices of AHF before the1998 dual-embassy attacks. Searches conducted by authorities revealed that el-Hage possessed contact information for a senior AHF official who was head of AHF's Africa Committee, the overseeing authority for AHF's offices in Kenya and Tanzania.

- In early 2003, individuals affiliated with AHF in Tanzania discussed the status of plans for an attack against several hotels in Zanzibar. The scheduled attacks did not take place due to increased security by local authorities, but planning for the attacks remained active.

- Information made available to the U.S. as shows that AHF offices in Kenya and Tanzania provide support, or act for or on behalf of al-Qaida and AIM.

AL-HARAMAIN FOUNDATION (PAKISTAN)

- Sometime in 2000, an AHF representative in Karachi, Pakistan met with Zelinkhan Yandarbiev. The U.S. has designated Yandarbiev, and the1267 Committee has included him on its list because of his connections to al-Qaida. The AHF representative and Yandarbiev reportedly resolved the issue of delivery to Chechnya of Zenit missiles, Sting anti-aircraft missiles, and hand-held anti-tank weapons.

- Before the removal of the Taliban from power in Afghanistan, the AHF in Pakistan supported the Taliban and other groups. It was linked to the UBL financed and designated terrorist organization, Makhtab al-Khidemat (MK). In one instance, some time in 2000, the MK director instructed funds to be deposited in AHF accounts in Pakistan and from there transferred to other accounts.

- At least two former AHF employees who worked in Pakistan are suspected of having al-Qaida ties. One AHF employee in Pakistan is detained at Guantanamo Bay on suspicion of financing al-Qaida operations. Another former AHF employee in Islamabad was identified as an alleged al- Qaida member who reportedly planned to carry out several devastating terrorist operations in the United States. In January 2001, extremists with ties to individuals associated with a fugitive UBL lieutenant were indirectly involved with a Pakistani branch of the AHF.

- As of late 2002, a senior member of AHF in Pakistan, who has also been identified as a "bin Laden facilitator," reportedly operated a human smuggling ring to facilitate travel of al-Qaida members and their families out of Afghanistan to various other countries.

- AHF in Pakistan also supports the designated terrorist organization, Lashkar E-Taibah (LET).

Identifier Information
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Tel. 021-8661-1265 and 021-8661-1266
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2-Garissa, Kenya
3-Dadaab, Kenya

AL-HARAMAYN FOUNDATION (TANZANIA)
1-P.O. Box 3616; Dar es Salaam, Tanzania
2 -Tanga
3 -Singida

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House #279, Nazimuddin Road, F-10/1, Islamabad, Pakistan

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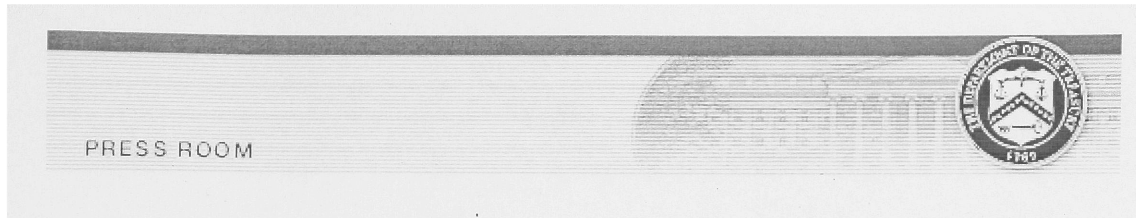


FROM THE OFFICE OF PUBLIC AFFAIRS

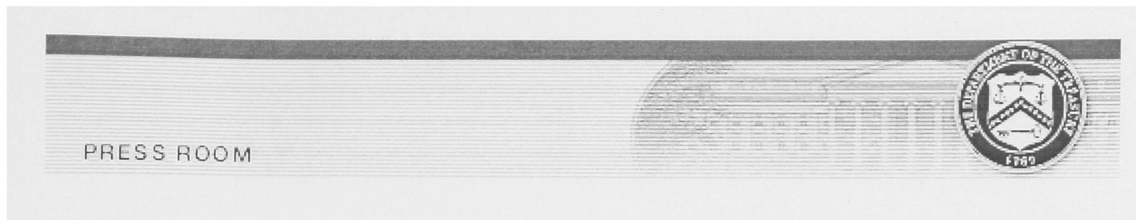
January 22, 2004
JS-1109

Secretary Snow To Visit Charleston, WV on Friday

Treasury Secretary John W. Snow will visit Charleston, WV on Friday, January 23 to meet with local business leaders and discuss the President's plan to further strengthen the U.S. economy through job creation.

During his visit to Charleston, Secretary Snow will tour a local construction site, an industry that is playing a key role in the growth of the U.S. economy. The Commerce Department this week reported that housing construction continued to increase in December, making 2003 the best year for home builders since 1978.

10:15 am Tour of Yorktown Development construction site
Lot 17 of Yorktown Subdivision
404 Buckingham Point
Charleston, WV
** tour is photo-op only; press availability will take place afterwards



FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1110

Remarks by Treasury Secretary John W. Snow at Second Annual Launch of IRS Free File Initiative

Good afternoon. Thank you all for joining us here today. I would like to thank OMB Director Bolten, IRS Commissioner Everson, and Mike Cavanagh with the Free File Alliance for joining me today as we launch the second year of "Free File".

The IRS's Free File Web site features private-sector software partners, the Free File Alliance, and allows most taxpayers to prepare and file their taxes online for free.
A substantial majority of citizens are eligible to use this innovative service at www.irs.gov. Free File is an exciting development in our efforts to make government more productive, efficient, and taxpayer-friendly. It furthers the President's vision and expectation that the government be run in a more businesslike manner.

Make no mistake--no one likes paying taxes—it's too confusing and too time consuming. But Free File makes this onerous task a good bit easier and less burdensome. Free File is an easy, fast and secure way for citizens to file taxes, and also allows Americans to get refunds in half the time. The efficiency of Free-file saves both taxpayers and the IRS money.

I would like to thank all of our Free File Alliance Members for their participation in providing millions of Americans the opportunity to file their taxes on line for free, and their commitment and efforts in improving the Free File system for the benefit of our customers--the taxpayers.

While tax simplification remains our goal, Free File incorporates a variety of features that reduce errors arising from the vast complexity of the tax code. In our technologically advanced economy, electronic transactions are everywhere. With this effort, the federal government is finally catching up to the nation we strive to support.

Last year, the IRS received 2.8 million e-filed returns through sixteen Free File Alliance members—this surpassed initial projections. This year, I hope that millions more will take advantage of Free File.

To encourage even more Americans to electronically file their taxes, the President's FY '05 budget will contain a proposal to extend the April filing date for electronic returns by fifteen days, to April 30th. This will give taxpayers a little extra time to get their affairs in order around tax day as an added inducement to e-file.

Congratulations to all at the IRS, and all the businesses involved in the Free File Alliance, for an important contribution to the future of the United States Government.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1111

Treasury Launches Financial Education Newsletter and Outlines Elements of a Successful Financial Education Program

The Treasury Department's Office of Financial Education (OFE) today released the first issue of its on-line, quarterly newsletter, ***The Treasury Financial Education Messenger***. The inaugural issue contains a message from Secretary John Snow stressing the importance of financial education as well as the eight elements of a successful financial education program.

"Financial education is extremely important for all Americans. As the President's Jobs and Growth Plan puts more money into the hands of consumers through lower marginal tax rates, an increased child tax credit, and accelerated marriage penalty relief, Americans have an even greater chance to save, invest, or spend extra money wisely. Yet without access to financial education resources, many people may miss out on this golden opportunity," said Secretary John Snow.

The eight elements of a successful financial education program in this edition of ***The Messenger*** offer guidance to financial education organizations as they develop programs and strategies to achieve the greatest impact in their communities. Each element is classified as relating to the program's content, delivery, impact or sustainability.

A successful program...	
Content	1. focuses on **basic savings**, **credit management**, **home ownership** and/or **retirement planning**.
	2. is **tailored to its target audience**, taking into account its language, culture, age and experience.
Delivery	3. is offered through a **local distribution channel** that makes effective use of community resources and contacts.
	4. follows up with participants to reinforce the message and ensure that participants are able to apply the skills taught.
Impact	5. **establishes specific program goals** and uses performance measures to track progress toward meeting those goals
	6. **demonstrates a positive impact on participants' attitudes, knowledge or behavior** through testing, surveys or other objective evaluation.
Sustainability	7. **can be easily replicated** on a local, regional or national basis so as to have broad impact and sustainability.
	8. is **built to last** as evidenced by factors such as continuing financial support, legislative backing or

	integration into an established course of instruction.

The Treasury Financial Education Messenger is available online at www.treasury.gov/financialeducation, where visitors can also subscribe to receive future issues of the newsletter by e-mail.

The Department of the Treasury's Office of Financial Education was established in May 2002. The Office of Financial Education is responsible for focusing the department's financial education policymaking, and for ensuring coordination on financial education within the Department and all of its bureaus. The Office of Financial Education serves to provide the Department of the Treasury with expertise on the many complex and interdisciplinary issues involved in financial education, and is able to tap into the Department's wide base of expertise on finance.

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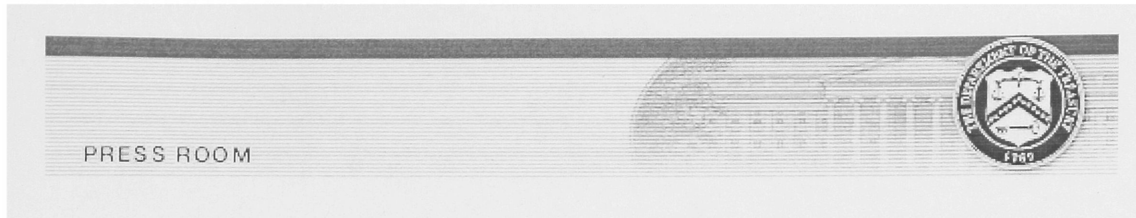

FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1112

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky

We are pleased to see today's report on the decline in initial unemployment insurance claims. It is additional evidence that the labor market is building strength and continuing to improve. New claims dropped last week, pushing the four-week moving average to its lowest point since January of 2001. Although this is encouraging news, there remains more to be done. This Administration is committed to strengthening the environment for job creation and will not be satisfied until every American looking for work can find a job.

Building on the progress started by the Jobs and Economic Growth Act, the President is continuing his efforts to strengthen the economy and create jobs, including the Jobs for the 21st Century initiative announced this week

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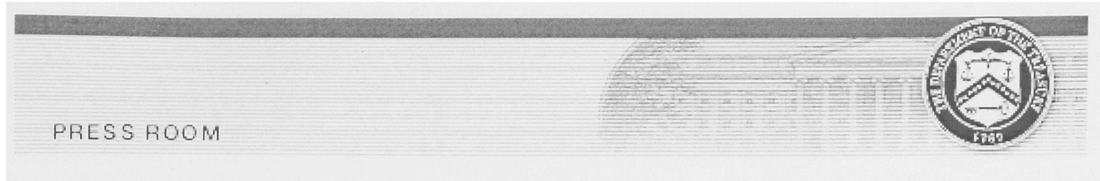

FROM THE OFFICE OF PUBLIC AFFAIRS

January 22, 2004
JS-1113

Photo: Secretary Snow announces the latest action in the financial war against terror

The United States joined with Saudi Arabia on Thursday to designate four branches of the Al-Haramain charitable organization in Kenya, Tanzania, Indonesia, and Pakistan for providing financial, material, or logistical support to terrorist organizations like al-Qaida

Media Contact

All media queries should be directed to the
Press Office at (202) 622-2960.
Only call this number if you are a member of the media.

High Resolution Image

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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January 23, 2004
JS-1114

Treasury and IRS Shut Down S Corporation ESOP Abuses

Today, the Treasury Department and the IRS issued a ruling to shut down abusive transactions involving "S corporation ESOPs." The ruling makes these "listed transactions" for tax-shelter disclosure purposes.

An employee stock ownership plan, or "ESOP," is a type of retirement plan that invests primarily in employer stock. Congress has allowed an "S corporation" to be owned by an ESOP, but only if the ESOP gives rank-and-file employees a meaningful stake in the S corporation. When an ESOP owns an S Corporation, the profits of that corporation generally are not taxed until the ESOP makes distributions to the company's employees when they retire or leave the job. This is an important tax break which allows the company to reinvest profits on a tax-deferred basis, for the ultimate benefit of employees who are ESOP participants.

The ruling shuts down transactions that move business profits of the S corporation away from the ESOP, so that rank-and-file employees do not benefit from the arrangement. For example, the ruling prohibits using stock options on a subsidiary to drain value out of the ESOP for the benefit of the S corporation's former owners or key employees.

"Congress recognized the potential for attempts to circumvent the rules and specifically authorized Treasury and IRS to prevent it. This notice does just that, imposing a 50% excise tax on the option holders in cases where rank-and-file ESOP participants are deprived of the business profits," stated Treasury Assistant Secretary for Tax Policy Pam Olson.

The text of Revenue Ruling 2004-4 is attached.

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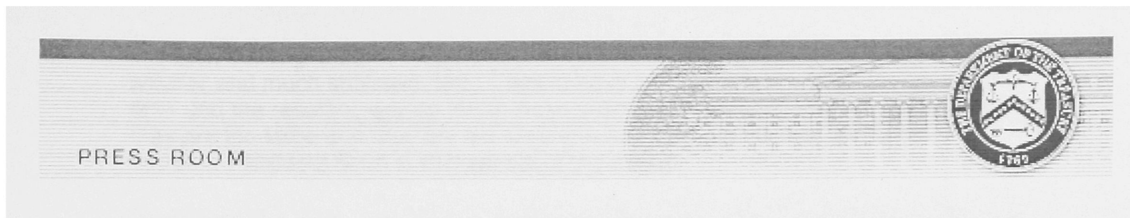
Related Documents:

- Revenue Ruling 2004-4



FROM THE OFFICE OF PUBLIC AFFAIRS

January 26, 2004
JS-1115

Remarks by U.S. Treasury Secretary John Snow to the Enterprise Conference -- "Advancing Enterprise: Britain in a Global Economy," London, UK (via satellite)

Good afternoon. I would like to thank Chancellor Gordon Brown for assembling such an illustrious group of participants for today's forum.

Today I want to talk about the joint responsibility the US and EU share in promoting a dynamic, growing world economy. The US and EU share particular challenges and we can be most effective when we work together to address them.

Cooperation by the G-8 to promote global growth and stability is at the top of G-8 agenda this year when the U.S. hosts the leaders Summit at Sea Island. The following year, when Prime Minster Blair will chair the leaders Summit, I hope we can be in a position to note substantial progress across all of our economies. The need for increased global economic growth, by the way, will be the top agenda item at the upcoming G7 meeting I will chair in Florida and the number one topic of discussion.

Let me provide a brief overview of our domestic situation. The US economy has faced tough challenges over the last three years -- 9-11, the collapse of the dotcom bubble, two wars, and corporate scandals. Yet we have managed to emerge with the shortest and shallowest cyclical downturn in the last 50 years, even while other major industrial economies were stagnant or declining.

Much of this is due to the fundamental strengths of the American economy and the American worker, whose productivity growth has averaged a 4.4% annual rate since the end of 2000, the fastest 11-quarter growth rate in 40 years (1963). It is also in large measure due to President Bush's tax cut package that put money in the hands of consumers when the economy needed it and set the basis for higher levels of capital formation and investment in the future.

But we are not satisfied with just weathering these storms. We are committed to policies that will support continued growth, prosperity and jobs in the US. President Bush has laid out an ambitious agenda for maximizing growth and job creation.

In his State of the Union speech, the President committed to making health care more affordable and its costs more predictable; working to prevent frivolous lawsuits from diverting money from job creation into legal battles; working to build a more affordable, reliable energy system; streamlining regulations and needless paperwork requirements; opening new markets to high value American products; preparing American workers for the demands of the 21st Century job market; and working to make tax relief permanent, so businesses and families alike can plan for the future.

All of these proposals point to the same end: create an environment that encourages flexibility, capital formation and innovation, and in turn leads to job creation, productivity, and higher living standards.

A word about our deficits. With the economic slowdown and recession that occurred in 2000 and 2001, the United States is experiencing a period of fiscal deficits. The

tax cuts, starting in 2001, were timely and effective; they made the recession much smaller and much shallower than it would have otherwise been. With the recession, 9/11 and the resulting war on terror these deficits are certainly understandable and they are too large and they are not welcome and they will not last. Make no mistake; President Bush is serious about the deficit.

We must keep the overall growth of spending down even as we bolster security and fight terror. The deficit, at roughly 4.5% of GDP, compared with 6% during the 80s, is not historically out of range. If we stick to President Bush's strong pro-growth economic policies and sound fiscal restraint, we expect to cut the deficit in half, toward a size that is below 2% of GDP, over the next five years.

Let me shed a little light on how the President will do this. In the budget that will be delivered to Congress on February 2nd, the President will propose holding discretionary nonsecurity-related spending accounts to a less than 1 percent increase. This will be the fourth consecutive year of slowing nonsecurity-related spending under this Administration. This is the lowest proposed rate of increase since 1993. This is below the rate of inflation. Additionally, total annually appropriated spending will increase by less than 4 percent next year.

Let me turn to particular challenges of interest to you in the EU.

For the EU, the challenge of increasing growth is most pressing for the major economies in Europe where growth has lagged and where estimates of growth potential are not as high as they should be. The EU has put forward the goal in its Lisbon Agenda of becoming the most competitive and dynamic economy by 2010. That's a most commendable objective and we in the US don't feel threatened by this growth. Quite the contrary, we'd like to see all the major economies striving to be dynamic, productive economies. Increased global economic growth will lead to mutually reinforcing success.

Simply put, we are not fighting for a piece of the pie, we are striving to enlarge the pie and improve standards of living for people in our economies and throughout the world. Your growth is important to us and our growth is important to you. Global growth is not a zero sum game. Lets do all we can to make sure we all grow together.

The EU still faces a number of challenges on the path to the Lisbon goals, as the Commission outlined the other day. But, there has also been real progress. I commend Germany for passing the difficult labor market and tax reforms as part of its Agenda 2010 and France for last year's pension reforms. We hope this is the bow wave of reform in Europe that boosts productivity and growth to new, higher levels.

Examples of growth oriented reform and its benefits can be found within the borders of the EU as well as outside. In a recent OECD study of industrial economies, the UK had the least restrictive regulatory regime in an index that combined barriers to trade, administrative regulation and economic regulation. It's no coincidence that the UK was able to avoid the major slowdown seen in other large European economies in the last few years or that it ranks with the US in leading industrial countries in information technology investment as a share of GDP, a key to productivity growth.

The EC's own findings also show a clear path for how to improve productivity, namely lowering regulation, increasing expenditures on research and development, completing the integration of markets and promoting EU competition, and reforming financial services so that capital markets can respond to these policies by directing finance to dynamic, employment-producing enterprises.

Cooperation between the US and the EU can enhance each of our growth agendas and promote broader growth. Let me dwell on two areas when our cooperation can yield significant results - free trade and financial sector integration.

Free Trade

With the dramatic expansion of trade in recent decades, the world economy is more connected than ever before.

For the United States, this means that our success in creating jobs and sustained economic growth depends in no small measure on opening markets and reducing barriers to trade. The same is true for the EU. It is through free trade that all nations can benefit from each other's prosperity. Free trade means new markets for exporters while companies and consumers benefit from lower-priced imports.

Obviously, both the United States and EU and many others were disappointed in the Cancun outcome, but there are hopeful signs that we can get the Doha Development Agenda back on track again so that 2004 is not a lost year. But even as we ponder the next steps in the WTO, the United States continues to press an aggressive trade agenda to open markets regionally and bilaterally with willing partners. By moving forward on multiple fronts, we can exert leverage for openness and create a new competition for trade liberalization. Just yesterday, we completed trade talks with Costa Rica ensuring they will be part of the Central American Free Trade Agreement. And today, we begin negotiations with Bahrain.

The focus of the WTO negotiations should be the market access agenda -- agriculture, industrial and consumer goods, and services. I believe that the United States and EU agree that these areas have the greatest potential to promote economic growth. Given that services were first included in multilateral trade talks in the last round, the US and EU are particularly interested in raising the number of countries with services commitments and the quality of those commitments, including in financial services.

The Doha Development Agenda also places particular emphasis on integrating the developing world into the global economy so that they may begin to reap the great benefits of free trade. The United States, the EU, Canada, and many others, including the World Bank, share the view that developing countries need to reduce their own trade barriers substantially in order to realize these benefits.

US/EU Financial Markets Dialogue

The US and EU markets represent the lion's share of global capital flows, making the US-EU financial relationship critical to well-functioning global financial markets, and the positive implications that entails for saving, investment and growth.

US Treasury and European Commission financial officials, along with our financial regulators, have been working actively during the past two years through our Informal Financial Markets Dialogue to resolve problems caused by law or regulation to allow capital to flow more efficiently.

Our dialogue has focused on the European Commission Financial Services Action Plan (FSAP), an ambitious effort to quickly build the legal and policy infrastructure for an integrated European capital market. The US has a profound interest in its success both to promote faster growth in Europe and a more robust transatlantic capital market that rewards competition and innovation. We also have an interest in seeing that US financial institutions in Europe will be able to compete fairly in the integrated European capital market. The EU also cares deeply about financial market developments in the US, including corporate governance issues and audit oversight. Together we also are addressing issues such as the supervision of large complex financial institutions, the evolution of Basle II and clearing and settlement processes.

It is not always easy. Both sides have different legal, historical, and cultural traditions. Recognizing this, our overarching goal in the financial markets dialogue is to see through these differences, and to achieve our common objectives in substance. We know that if this process is managed successfully, it is a win-win for the US, Europe and the world.

Thank you.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 27, 2004
JS-1116

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on January Consumer Confidence

Increasing consumer confidence levels are an encouraging sign as the economy continues to gain strength. Following a ten-point jump in the University of Michigan's Consumer Sentiment Index earlier this month, January's Consumer Confidence Index reached its highest point in 18 months.

The positive mood reflects the success of the President's economic policies as well as encouraging news in many areas of the economy such as housing, manufacturing and business investment. Despite the increasing signs of good news, there is more work to be done. This Administration will continue in its efforts to create a stronger environment for job creation and will not be satisfied until every American looking for work can find it.

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PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 27, 2004
JS-1117

Treasury Announces Departure of Gary B. Wilcox

Today the Treasury Department announced that Gary B. Wilcox, Deputy Chief Counsel (Technical) for the Internal Revenue Service, will leave the Office of Chief Counsel in mid-February and return to private practice.

Mr. Wilcox joined the IRS in February 2002 as principal deputy to B. John Williams, the former Chief Counsel. Having primary responsibility within the IRS for the development of the Service's positions on technical tax issues and the issuance of regulations and rulings, Mr. Wilcox was instrumental in carrying out Chief Counsel Williams' and Treasury's priority of issuing more published guidance for the benefit of taxpayers, tax professionals and IRS agents. During Mr. Wilcox's tenure, the rate of published regulations and rulings increased significantly in comparison to prior years.

"The tax system has been incredibly fortunate to have Gary's service during challenging times. Gary brought to the Office of Chief Counsel his outstanding ability as a lawyer, a common sense appreciation of the circumstances in which taxpayers and IRS agents must operate, management skills, and above all good judgment," said Treasury Assistant Secretary for Tax Policy Pam Olson. "We could not have accomplished what we have the last two years without Gary's contributions to the guidance process and to addressing the compliance problems facing the tax system. He will be sorely missed."

"Gary's contributions to improving IRS public guidance have been extraordinary. Taxpayers, practitioners and tax administrators all owe Gary their gratitude for his willingness to use his exceptional legal talent in public service the past two years," stated B. John Williams, former Chief Counsel for the IRS and currently a tax partner with Shearman & Sterling.

Mr. Wilcox will be rejoining his former law firm, Morgan Lewis, where he will maintain offices in both Philadelphia and Washington, D.C.

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FROM THE OFFICE OF PUBLIC AFFAIRS

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January 28, 2004
JS-1118

Statement of Secretary John W. Snow on the Departure of Assistant Secretary for Management & Chief Financial Officer Teresa Ressel's

"Assistant Secretary Ressel has served a key role in President George W. Bush's administration. Her involvement in the establishment of a new Department of Homeland Security (DHS) – the largest reorganization of Federal Government in half a century – was particularly noteworthy.

"The creation of DHS was a big job for our department, since it involved so many of the Treasury Department's agencies. Assistant Secretary Ressel worked hard to make that transition a smooth one for everyone involved. Additionally, her work has helped Treasury's financial management performance continue to lead government, and she helped Treasury complete an outstanding FY2003 financial closure. She departs with the sincere gratitude and best wishes of all of her colleagues here at Treasury."

Related Documents:

- Ressel Letter

DEPARTMENT OF THE TREASURY
WASHINGTON

ASSISTANT SECRETARY

January 27, 2004

The President
The White House
Washington, D.C. 20500

Dear Mr. President,

It has been my privilege and honor to serve you and our country since August of 2001. Unfortunately, the demands of this role make it extremely challenging to spend virtually any time with my family and children Thus, I respectfully would like to return to the private sector to spend more time with them, and I am writing to resign as Assistant Secretary of the Treasury for Management

To allow for a smooth transition, Secretary Snow and I have agreed that my resignation take effect during February.

Your leadership to clearly establish the President's Management Agenda created an opportunity for the Management functions in government to align resources with results Treasury accomplishments in financial management and performance have driven change across the government on this aspect of your Agenda. In parallel, your 2003 priority of establishing the Department of Homeland Security offered an opportunity for the Treasury Management function to contribute in a very significant way and support the stand-up of that enterprise. Literally, hundreds of colleagues contributed to this effort and I am proud of our contributions both relative to human capital and change management.

However, as you wonderfully stated at your leadership talk on January 9,2004 – there is always much more to accomplish. While we have made significant progress, I am very proud of the management team assembled at Treasury to drive future accomplishments as well.

I will always remember and honor the opportunity to serve under your leadership

Very truly yours,

Teresa M. Ressel

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

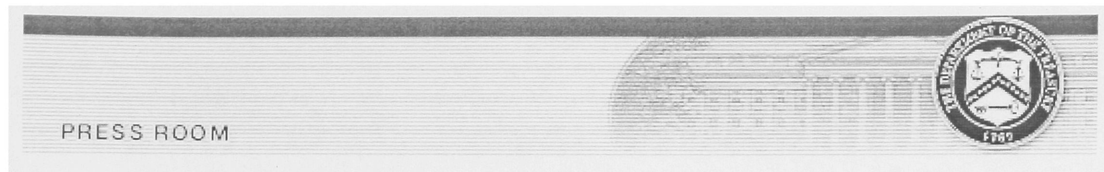
January 28, 2004
JS-1119

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on Home Sales

The strength of the housing sector continues to bolster the economy. New home sales in 2003 topped 2002 by nearly 12 percent to reach the best year on record. This follows a report earlier this week which found existing home sales also set a record in 2003, posting an almost 10 percent gain over 2002.

Record-breaking home sales build on encouraging news in housing construction. Last week's report on housing starts found them reaching a twenty-year high in December.

While we are pleased by the continuing strength of the housing sector, as well as many other areas of the economy, we are not satisfied. Remaining steadfast in this Administration's commitment to improving the environment for job creation, the President will continue in his efforts to ensure that every American looking for work can find a job.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 28, 2004
JS-1120

Treasury to Host Inaugural Meeting of the Financial Literacy and Education Commission

The Department of the Treasury tomorrow will host the inaugural meeting of the Financial Literacy and Education Commission. The Commission was established by the Fair and Accurate Credit Transactions Act, signed by President Bush on December 4, 2003. The Commission will work to promote and improve financial education by coordinating the many efforts underway at the 20 participating government agencies. The legislation designated that the Secretary of the Treasury serve as the Chairperson of the Commission and that Treasury's Office of Financial Education provide primary support to the Commission.

Tomorrow's event will include opening remarks from Secretary Snow, followed by remarks from Chairman Alan Greenspan and other commission members. Agencies that are members of the Commission are listed below.

WHAT: Inaugural Meeting of the Financial Education and Literacy Commission

WHEN: Thursday, January 29, 2004
10:30 am EST

WHERE: Department of the Treasury, Cash Room

WHO: Secretary John W. Snow, Department of the Treasury
Chairman Alan Greenspan, Chairman of the Federal Reserve Board of Governors Representatives of the other Commission Members: Office of the Comptroller of the Currency; the Office of Thrift Supervision; the Federal Reserve; the Federal Deposit Insurance Corporation; the National Credit Union Administration; the Securities and Exchange Commission; the Departments of Education, Agriculture, Defense, Health and Human Services, Housing and Urban Development, Labor, and Veterans Affairs; the Federal Trade Commission; the General Services Administration; the Small Business Administration; the Social Security Administration; the Commodity Futures Trading Commission; and the Office of Personnel Management.

Tomorrow's meeting will be webcast live at www.treasury.gov

Media without Treasury press credentials planning to attend today's event should contact the Treasury Public Affairs office at 202/622-2960 with the following information: name, social security number and date of birth. Media with White House press credentials must call to be cleared in to the Treasury Building. Please plan to arrive at least 30 minutes early.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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January 28, 2004
js-1121

Treasury and IRS Propose New Tax Form For Corporate Tax Returns

In an effort to increase the transparency of corporate tax return filings, today the Treasury Department and Internal Revenue Service released a new proposed draft form, Schedule M-3, Net Income (Loss) Reconciliation for Corporations with Total Assets of $10 Million or More, for use by certain corporate taxpayers filing Form 1120, U.S. Corporation Income Tax Return. The new Schedule M-3 would expand the current Schedule M-1, which has not been updated in several decades.

Schedule M-1 reconciles a corporation's financial accounting income or loss with the taxable income or loss reported on the Form 1120. Large and Midsize Business (LMSB) taxpayers (those with total assets of $10 million or more) will complete the new Schedule M-3 in lieu of completing Schedule M-1. Small Business and Self-Employed (SB/SE) taxpayers will not be required to complete the new Schedule M-3 and will continue to complete Schedule M-1. Other federal tax returns that also require the completion of Schedule M-1 (e.g., Form 1065, U.S. Partnership Return of Income, and Form 1120S, U.S. Income Tax Return for an S Corporation) may incorporate Schedule M-3 in the future.

"The proposed Schedule M-3 will make differences between financial accounting net income and taxable income more transparent. This will help agents determine from the return whether the return should be audited and identify the differences that matter most in the audit of the return. We see benefits to taxpayers and the IRS from the new Schedule: a reduction in unnecessary audits and a swifter focus on those differences that are more likely to arise when taxpayers take aggressive positions or engage in aggressive transactions. In addition, the increased transparency will have a deterrent effect," stated Treasury Assistant Secretary for Tax Policy Pam Olson.

"The new Schedule will let the IRS sharpen and improve monitoring of corporate compliance," said IRS Commissioner Mark W. Everson. "Our objective is to identify and resolve potential audit issues promptly. This information will help us do so."

"These changes will enable us to focus our compliance resources on returns and issues that need to be examined and avoid those that do not," said Deborah M. Nolan, IRS Large and Mid-Size Business Division Commissioner. "Increasing the transparency of corporate tax returns is critical to our objectives to provide certainty to taxpayers sooner and to improve overall compliance."

The Treasury and IRS expect that the proposed Schedule M-3 will be finalized for use with federal income tax returns for tax years ending on or after December 31, 2004.

The draft Schedule M-3, along with a general description of Schedule M-3, is attached and may be accessed on www.irs.gov. Instructions for Schedule M-3 will be released in the future and will be available on www.irs.gov.

Comments are requested regarding proposed Schedule M-3, including comments on ways to minimize taxpayer burden. In addition, comments are requested on significant difficulties that taxpayers may encounter if the use of Schedule M-3 is required for a tax year that begins before Schedule M-3 is finalized. Comments

should be submitted by April 30, 2004 to:

Susan Blake
Internal Revenue Service
Office of Pre-Filing and Technical Guidance
1111 Constitution Ave. NW
Mint Bldg M3-353 LM:PFT
Washington, DC 20224
Telephone number 202-283-8414
email address: PFTG2@irs.gov

ATTACHMENTS:
Draft Schedule M-3
Schedule M-3 General Explanation

-30-

Related Documents:

- Draft Schedule M-3
- Schedule M-3 General Explanation

SCHEDULE M-3 (Form 1120)

Department of the Treasury
Internal Revenue Service

Net Income (Loss) Reconciliation for Corporations With Total Assets of $10 Million or More

▶ Attach to Form 1120.
▶ See separate instructions.

OMB No. 1545-XXXX

2004

Name

Employer identification number

Part I **Questions Regarding Corporate Financial Statements and Publicly Traded Common Stock**

1 Indicate source of net income shown on Part II, line 1:
- a ☐ SEC Form 10-K
- b ☐ Other certified GAAP income statement
- c ☐ Other income statement
- d ☐ No income statement. Books and records used.

Note: *If line 1d is checked, skip lines 2 through 5 of Part I, skip lines 1 through 7 of Part II, and enter net income (loss) per books and records of includible corporations on line 8 of Part II.*

2 What is the income statement period for net income shown in Part II, line 1? From ___/___/___ To ___/___/___

3 In the current or past five years, have the corporation's financial statements been restated? . . . . ☐ **Yes** ☐ **No**
(If yes, attach details)

4 Under what symbol does the corporation's common stock trade? ________ On what exchange does it trade? ________

5 What is the nine-digit CUSIP number of the corporation's publicly traded common stock? ☐☐☐☐☐☐☐☐☐

Part II **Reconciliation of Net Income (Loss) per Income Statement With Net Income (Loss) of Includible Corporations**

1	**Net income (loss) per income statement**	1	
2	Remove net income (loss) of nonincludible foreign corporations (attach schedule)	2	
3	Remove net income (loss) of nonincludible U.S. corporations (attach schedule)	3	
4	Include net income (loss) of other includible corporations (attach schedule)	4	
5	Adjust elimination of transactions between includible and nonincludible corporations (attach schedule)	5	
6	Adjust net income (loss) to reconcile income statement year to tax return year (attach schedule)	6	
7	Other adjustments required to reconcile to amount on line 8 (attach schedule)	7	
8	**Net income (loss) per income statement of includible corporations. Add lines 1 through 7**	8	

Part III Reconciliation of Net Income (Loss) per Income Statement of Includible Corporations With Taxable Income per Return—Income (Loss) Items

	Income (Loss) Items	(A) Income (Loss) per Income Statement	(B) Temporary Difference	(C) Permanent Difference	(D) Income (Loss) per Tax Return
1	Income (loss) from equity method foreign corporations				
2	Gross foreign dividends not previously taxed				
3	Subpart F, PFIC, QEF, and similar income inclusions				
4	Section 78 gross-up				
5	Gross foreign distributions previously taxed				
6	Income (loss) from equity method U.S. corporations				
7	U.S. dividends not eliminated in tax consolidation				
8	Minority interest for includible corporations				
9	Income (loss) from U.S. partnerships (attach schedule)				
10	Income (loss) from foreign partnerships (attach schedule)				
11	Income (loss) from other flow-through entities (attach schedule)				
12	Tax-exempt interest				
13	Life insurance proceeds				
14	Involuntary conversions				
15	Like-kind exchanges				
16	Hedging transactions				
17	Section 481(a) adjustments				
18	Inventory valuation adjustments				
19	Section 198 environmental remediation costs				
20	Other amounts relating to reportable transactions (attach details)				
21	Sale versus lease				
22	Mark-to-market income (loss)				
23	Unearned revenue/advance receipts				
24	Installment sales				
25	Long-term contracts				
26	Original issue discount				
27	Net capital gain from flow-through entities				
28	Net capital loss from flow-through entities	( )			( )
29	Gross capital gain from includible corporations				
30	Gross capital loss from includible corporations	( )			( )
31	Disallowed capital loss in excess of capital gains				
32	Utilization of capital loss carryforward				
33	Other income (loss) items with differences (attach schedule)				
34	Other income (loss) items with no differences				
35	**Total income (loss) items.** Add lines 1 through 34				
36	**Total expense/deduction items (from Part IV, line 38**				
37	**Reconciliation totals: Subtract line 36 from line 35**				
	Note: *Line 37, Column A must equal amount on Part II, line 8 and Column D must equal amount on Form 1120, page 1, line 28.*	**Net Income (loss) per income statement, Part II, Line 8**	**Net Temporary Differences**	**Net Permanent Differences**	**Taxable Income (Loss), (Form 1120) Page 1, line 28**

Part IV Reconciliation of Net Income (Loss) per Income Statement of Includible Corporations With Taxable Income per Return—Expense/Deduction Items

	Expense/Deduction Items	(A) Expense per Income Statement	(B) Temporary Difference	(C) Permanent Difference	(D) Deduction per Tax Return
1	U.S. current tax expense				
2	U.S. deferred tax expense				
3	State current tax expense				
4	State deferred tax expense				
5	Foreign current tax expense				
6	Foreign deferred tax expense				
7	Foreign withholding taxes				
8	Stock option (ISO)				
9	Stock option (NQSO)				
10	Restricted stock				
11	Meals and entertainment				
12	Fines and penalties				
13	Nondeductible punitive damages				
14	Excess parachute payments				
15	Excess section 162(m) compensation				
16	Charitable contribution of cash and tangible property				
17	Charitable contribution of intangible property				
18	Charitable contribution limitation				
19	Charitable contribution carryforward used				
20	Current year acquisition/reorganization investment banking fees				
21	Current year acquisition/reorganization legal/accounting fees				
22	Current year acquisition/reorganization other costs				
23	Impairment of goodwill				
24	Amortization of acquisition/reorganization and start-up costs				
25	Other amortization or impairment write-offs				
26	Abandonment losses (attach details)				
27	Worthless stock deduction (attach details)				
28	Depletion				
29	Depreciation				
30	Bad debt expense				
31	Accrued non-deductible liabilities (attach details)				
32	Corporate owned life insurance premiums				
33	Section 481(a) adjustments				
34	Inventory valuation adjustments				
35	Other amounts relating to reportable transactions (attach details)				
36	Other expense/deduction items with differences (attach schedule)				
37	Other expense/deduction items with no differences				
38	**Total expense/deduction items.** Add lines 1 through 37. Enter here and on Part III, line 36				

General Description of Schedule M-3: Net Income (Loss) Reconciliation for Corporations With Total Assets of $10 Million or More

Background

- The current Schedule M-1 has remained virtually unchanged for decades. Over that same period of time, large and midsize corporations have changed dramatically in the ways they are structured and conduct business, and in their corresponding financial and tax accounting.
- Schedule M-1 (and the related instructions) do not provide a uniform reporting requirement for "net income per books" on line 1 of Schedule M-1. As a result, taxpayers may provide information for (i) the worldwide group, (ii) the U.S. consolidated tax group, or (iii) something in between.
- Similarly, Schedule M-1 (and the related instructions) do not provide uniform disclosure requirements for reporting differences between financial accounting net income and taxable income. The lack of requirements prevent efficient comparisons among taxpayers and from year to year for the same taxpayer, thus making assessment of the risk of noncompliance associated with an issue or a taxpayer more difficult.

Goals of Schedule M-3

- Increase transparency while minimizing overall taxpayer burden.
- Reduce the time required to examine tax returns and be in a position to examine the most recent tax returns filed.
- Provide consistent reporting among taxpayers and from year to year for each taxpayer.
- Provide a method of presentation to obtain more useful, descriptive information at the time the federal income tax return is filed to assist the IRS in the identification of tax returns that should or should not be selected for audit, identification of issues that should or should not be audited, and identification of trends and areas of greater compliance risk.
- Periodically modify the form to highlight emerging issues, identify trends, and adapt to future changes encountered by large and midsize corporations.
- Facilitate tax return selection and issue identification through electronic filing.
- Facilitate the use of Limited Issue Focused Examination (LIFE) audits through greater transparency.

Highlights of Schedule M-3

Who is affected?

- Only Large and Midsize Business (LMSB) corporate taxpayers reporting gross assets of $10 million or more on Schedule L (balance sheet) on Form 1120 at the end of the taxable year would be required to complete and file Schedule M-3 instead of Schedule M-1.
- All other taxpayers would continue to complete and file Schedule M-1. No changes are proposed for Schedule M-1 at this time.
- It is expected that a form similar to Schedule M-3 will be designed for Form 1065 Partnership Income Tax Returns, Form 1120S Small Business Corporation Income Tax Returns, and perhaps other federal income tax returns that warrant enhanced transparency.

Specifics of Schedule M-3

Part I – Question regarding corporate financial statements and publicly traded common stock

Part 1 asks questions to identify the source of the financial statement information. Taxpayers would be required to reconcile financial accounting net income to taxable income based on the following hierarchy:

- SEC Form 10-K financial statements;
- Other certified GAAP statements;
- Other financial statements (with explanation of accounting method attached); and
- If no financial statements are prepared by the taxpayer (certified or otherwise), then the taxpayer would report income from its books and records on the last line (Line 8) of Part II and skip the other lines.

Part II – Reconciliation of net income (loss) per income statement with net income (loss) of includible corporations

Part II is a consolidated schedule that reconciles the taxpayer's worldwide net income (loss) per the income statement (as determined in Part I (for example, the income statement per the financial statements if one is prepared by the taxpayer)) to the net income (loss) of the corporations included in the U.S. tax return (the U.S. consolidated tax group).

- (Line 1) Start with net income (or loss) per the income statement.
- (Line 2) Remove net income (or loss) of foreign corporations that are included in Line 1, but not in the U.S. consolidated tax group.

- (Line 3) Remove net income (or loss) of U.S. corporations that are included in Line 1, but not in the U.S. consolidated tax group (for example, 51% to 79%-owned U.S. subsidiaries).

- (Line 4) Include net income (or loss) of corporations that are consolidated for federal income tax purposes, but are not included on Line 1.

- (Line 5) Adjust (remove or include) eliminations of intercompany transactions that relate to non-includible entities removed in lines 2 and 3 or included in line 4, leaving only intercompany eliminations that relate to includible entities. Generally, for those corporations removed on Lines 2 and 3, Line 5 will add back dividends received by the U.S. consolidated tax group and adjust for minority interests included on Lines 2 or 3.

- (Line 6) Include adjustments for differences between the taxpayer's income statement year and tax return year.

- (Line 7) Include any other necessary adjustments and attach a detailed schedule of those adjustments.

- (Line 8) Line 8 is the net income (or loss) per the income statement of the consolidated tax group. Taxpayers that did not prepare financial statements would enter net income (or loss) per books and records for the U.S. consolidated tax group.

The instructions to Part II would clarify that any amounts reported on Lines 2-7 must be separately stated and adequately disclosed and the combining, or netting, of amounts is not permitted.

<u>Part III and IV– Reconciliation of net income (loss) per income statement of includible corporations with taxable income per return.</u>

Part III and IV are consolidating schedules that reconcile the net income (or loss) per the income statement of the U.S. consolidated tax group in Part II Line 8 to the taxable income of the U.S. consolidated tax group on Form 1120, Page 1, Line 28.

- Part III breaks out differences (between the net income (or loss) per the income statement and taxable income) in items usually considered to be income (or loss) items.

- Part IV breaks out differences (between the net income (or loss) per the income statement and taxable income) in items usually considered to be expense/deduction items.

- Any income (or loss) items in Part III, or any expense/deduction items in Part IV, that do not result in a difference between net income (or loss) per the income statement and taxable income are reported on a single line in each respective part.

- Part III and IV require the taxpayer to identify the portion of each difference that is a permanent difference and the portion that is a temporary difference. Generally, items of difference that will reverse (that is, have an opposite effect on taxable income in later years due to the difference in timing of recognition for accounting and federal income tax purposes) or that are a reversal of prior differences are temporary differences, and items that will never reverse are permanent differences.

- The specific differences listed in Part III and IV reflect:
  - ➢ low risk differences that are separated out for greater transparency,
  - ➢ high risk differences that may require attention, and
  - ➢ other areas of special concern such as emerging issues.

- The instructions to Part III and Part IV will clarify that any difference reported must be separately stated and adequately disclosed.

- Part III and IV each conclude with a summation of each of the columns. The total of each column in Part IV is reported on a separate line at the bottom of Part III.
  - ➢ The first column of Part III is the net income per the income statement and must equal the amount shown at Part II Line 8.
  - ➢ The second column is the total of all temporary differences.
  - ➢ The third column is the total of all permanent differences.
  - ➢ The fourth column is taxable income and must equal the amount shown at Form 1120, Page 1, Line 28.

Schedule L

- No changes are proposed to the format of Schedule L (the balance sheet) of Form 1120 at this time.
- The Form 1120 instructions would clarify that:
  - ➢ The balance sheet amounts on Schedule L reflect full consolidation accounting for all entities that are included in the tax return (with full elimination of intercompany transactions between all includible entries), and not some form of combination accounting.
  - ➢ The balance sheet amounts on Schedule L should correspond to the taxpayer's financial statement amounts, if financial statements are prepared (in the case of a U.S. consolidated tax group, if financial statements are prepared for the U.S. parent).
  - ➢ The balance sheet amounts on Schedule L should not be tax-basis balance sheet amounts, unless the taxpayer only keeps tax-basis books and records and reconciles to taxable income from net income per books and records rather than from some financial statement net income amount.

FROM THE OFFICE OF PUBLIC AFFAIRS

January 29, 2004
js-1122

Secretary Snow Chairs First Meeting of the Financial Literacy and Education Commission

Secretary of the Treasury John Snow today chaired the first meeting of the Financial Literacy and Education Commission in the Department of the Treasury's Cash Room. Representatives of twenty federal departments, agencies, and commissions, including Federal Reserve Board Chairman Alan Greenspan, Federal Deposit Insurance Corporation Chairman Donald Powell, Federal Trade Commission Chairman Timothy Muris, Office of Thrift Supervision Director James Gilleran, Social Security Administration Commission Jo Anne Barnhart, and National Credit Union Administration Chairman Dennis Dollar, participated in the meeting.

"Financial Literacy is the often the key to financial security. By coordinating our many ongoing efforts and joining forces with the financial literacy community, the Commission can work together, learn from each other and discover how we can best succeed in our efforts to make Americans aware of the many benefits of our financial system including opportunities to save, plan for the future, use credit wisely and purchase a first home," said Secretary Snow.

At the inaugural meeting today, the members of the Commission discussed the establishment of subcommittees to fulfill two of the legislation's charges: to establish and maintain a toll-free telephone number for financial education purposes; and establish and maintain a financial education website that will serve as a central clearinghouse for citizens who are in search of financial education information and programs.

The new Commission's goal is to promote financial education and improve the financial literacy of all Americans. The Commission will work to encourage government and private sector efforts to promote financial literacy, and coordinate financial education efforts of the federal government, including the identification and promotion of best practices.

The legislation that created the Financial Literacy and Education Commission calls for the development of a national strategy to promote financial literacy and education among all American consumers; establishment of a website to serve as a clearinghouse and provide a coordinated point of entry for information about federal financial literacy and education programs, grants, and other information the Commission finds appropriate; and the establishment of a toll-free hotline available to members of the public seeking information about issues pertaining to financial literacy and education.

The Financial Literacy and Education Commission was created by Title V of the Fair and Accurate Credit Transactions Act, signed by President Bush on December 4, 2003. The Commission is composed of the Secretary of the Treasury and the heads of the Office of the Comptroller of the Currency; the Office of Thrift Supervision; the Federal Reserve; the Federal Deposit Insurance Corporation; the National Credit Union Administration; the Securities and Exchange Commission; the Departments Education, Agriculture, Defense, Health and Human Services, Housing and Urban Development, Labor, and Veterans Affairs; the Federal Trade Commission; the General Services Administration; the Small Business

Administration; the Social Security Administration; the Commodity Futures Trading Commission; and the Office of Personnel Management.

The Treasury Department's Office of Financial Education has been designated by Congress to lend its expertise and provide primary support to the Commission to assist it in fulfilling its functions and duties. The Office of Financial Education (OFE) was established in May 2002, as part of the Treasury Department's long-term commitment to ensure that all Americans have access to financial education programs that will help them make informed financial decisions throughout their lives. More information about the OFE can be found at: www.treasury.gov/financialeducation.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 29, 2004
JS-1123

Remarks by Treasury Secretary John W. Snow
Financial Literacy and Education Commission
Inaugural Meeting

Good morning, and welcome, everyone, to the Department of the Treasury. It's always a pleasure to bring guests to this historic building, and particularly to this incredible room.

The group who has gathered here today is impressive by anyone's standards.

It strikes me that any cause, any organization, would be honored, and fortunate to attract just one or two of these individuals to work and speak on its behalf.

I'm pleased to say that this fine group of men and women are here today because they are all dedicated to Financial Literacy.

So, welcome: Chairman Greenspan, Chairman Powell, Chairman Muris, Director Gilleran, Commissioner Barnhart, Chairman Dollar and the representatives of the other Commission members.

Welcome, and thank you for your commitment to this issue that is fundamentally important to all Americans. I'm extremely proud that President Bush and his administration are so dedicated to this cause.

It has been said that, regardless of how much money you have, wisdom has to be acquired on the installment plan.

Similarly, it is true that regardless of an individual's income, saving must be done steadily, deliberately, over a lifetime.

Learning about how to become, and stay, financially healthy, is a life-long pursuit as well.

And that's why we're here today.

So many individuals and organizations – across the many agencies of government, among members of Congress, and throughout the private sector – are dedicating major resources to improve financial literacy in America.

In other words, there is a serious movement afoot, and it is a good one. And this commission is not intended to replace those efforts... but, rather, to complement them, act as a point of synergy for them, and of course to give them institutional support.

A bit of history behind today's inaugural meeting:

The Treasury Department's Office of Financial Education was created by this Administration in May of 2002.

Its work was then recognized by Congress in the same action that created this commission… that is: Title Five of the Fair and Accurate Credit Transactions Act, which the President signed this past December.

Treasury's Financial Education Office will serve as the supporting office for this new Commission.

Our work is to complement, encourage and sometimes coordinate the work of so many individuals and institutions that are committed to greater financial literacy in America. I would also like to see us identify some areas that need the most help, the quickest.

For example: we have a tremendous opportunity to start fresh with a new generation… to ensure that tomorrow's young adults understand how important it is to save, and how to protect themselves from identity theft, in the same way that they understand the basics of physical health or road safety.

There is a tremendous interest on the part of high school students to learn the financial facts of life: how to manage a credit card, how to save and invest, how important it is to save for retirement at the beginning of a career, not at the end.

When you consider the fact that the financial tragedy of bankruptcy is growing fastest among young adults in their early 20s, it becomes clear that we must work to satisfy the natural desire of young people to learn now and therefore reduce this problem for the next generation.

Another group that has an immediate need is our population of new immigrants to this country.

Many new immigrants come to America from places where consumer financial services are not common, where checking accounts and credit cards and mortgage loans are virtually unknown, and where a bank is not seen as a safe place to put your money. They do not know how to get involved in the financial mainstream here, and so they remain outside of the mainstream, prey to the loan sharks and the financial predators.

This commission, and anyone who is passionate about financial literacy, should reach out to these people to help bring them into the financial mainstream, where they can safely build up their assets, invest and save for their futures and their children's futures.

I'm excited to work with the esteemed members of this Commission to address these and other issues in the realm of financial literacy. I envision this Commission as a forum where we work together, where we learn from each other… ultimately discovering what works, what doesn't, and how we can best succeed.

Together, we will work with the financial literacy community in reaching out to the millions of people in the multitude of different ways that we collectively offer.

Thank you very much.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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January 29, 2004
JS-1124

Treasury and IRS issue Guidance on the Application of Income Tax Treaties to Service Partnerships

Today, the Treasury Department and the IRS issued guidance concerning the application of the U.S.-Germany income tax treaty to a nonresident partner in a service partnership that conducts activities in the United States. Revenue Ruling 2004-3 makes clear that a nonresident partner is subject to U.S. income taxation on his share of income from the partnership to the extent that such income is attributable to the partnership's activities in the United States, without regard to whether the partner performs services in the United States. The guidance in this revenue ruling also applies in the case of other U.S. income tax treaties that contain applicable provisions regarding independent personal services like the provisions in the U.S.-Germany income tax treaty.

Related Documents:

- The text of the Revenue Ruling

Part I
Section 894.—Income Affected By Treaty
26 CFR 1.894-1: Income affected by treaty
Rev. Rul. 2004-03

ISSUE

Whether a nonresident partner in a service partnership that has a fixed base in the United States is subject to U.S. tax on income attributable to that fixed base under Article 14, Independent Personal Services, of the Convention Between the United States of America and the Federal Republic of Germany for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital and to Certain Other Taxes, signed on August 29, 1989, as amended by the Protocol signed on the same date (the "Treaty").

FACTS

P is a service partnership that is organized under the laws of Germany. P has offices in Germany and the United States. Its U.S. office is a fixed base under Article 14 of the Treaty. P is comprised of two partners: A, a nonresident alien individual who is a resident of Germany under Article 4 of the Treaty, and B, a U.S. resident. A performs services solely at P's office in Germany and B performs services solely at P's office in the United States. A and B agree to divide the profits of the partnership equally.

LAW AND ANALYSIS

Under section 701 of the Internal Revenue Code (the "Code"), a partnership is not subject to income tax; rather, the persons carrying on the business of the partnership as partners are liable for income tax in their separate or individual capacities. Code section 702 requires a partner to determine its income tax by separately taking into account its distributive share of the partnership's income. Under section 702(b), the character of an item of income, gain, loss, deduction, or credit is determined as if such item were realized directly from the source from which it was realized by the partnership, or incurred in the same manner as incurred by the partnership. Under Code section 704, a partner's distributive share generally is determined by the partnership agreement unless an allocation under the agreement does not have substantial economic effect.

Under section 875(1) of the Code, a nonresident alien individual who is a partner in a partnership that is engaged in a U.S. trade or business is himself considered to be so engaged. Section 871(b)(1) of the Code provides that a nonresident alien individual is taxable under Code sections 1 or 55 on his taxable income that is effectively connected with the conduct of a U.S. trade or business.

Section 894(a)(1) states that the provisions of the Code shall be applied to any taxpayer with due regard to any U.S. treaty obligation that applies to such taxpayer. In Donroy, Ltd. v. United States, 301 F.2d 200 (9th Cir. 1962), the court held that the U.S. permanent establishment of a partnership was attributable to a foreign person that was a limited partner under the 1942 U.S.-Canada income tax treaty. In Unger v. Commissioner, 936 F.2d 1316,1319 (D.C. Cir. 1991), the court followed the holding in Donroy, noting that it stood for the proposition that the office or permanent establishment of a partnership is, as a matter of law, the office of each of the partners—whether general or limited. See also Johnston v. Commissioner, 24 T.C. 920 (1955) (holding that a partnership's permanent establishment is deemed to be a permanent establishment of its partners); Rev. Rul. 90-80, 1990-2 C.B. 170 (same).

Article 14 of the Treaty provides:

> 1. Income derived by an individual who is a resident of a Contracting State from the performance of personal services in an independent capacity shall be taxable only in that State, unless such services are performed in the other Contracting State and the income is attributable to a fixed base regularly available to the individual in that other State for the purpose of performing his activities.
>
> 2. The term "personal services in an independent capacity" includes but is not limited to independent scientific, literary, artistic, educational, or teaching activities as well as the independent activities of physicians, lawyers, engineers, economists, architects, dentists, and accountants.

Applying Article 14 in the partnership context requires a determination of whether an individual partner in a service partnership who derives income attributable to the fixed base of the service partnership in the other Contracting State is taxable on that income even though the partner does not perform any services in the other Contracting State. Consistent with section 875 and the case law discussed above, the fixed base of a partnership is attributed to its partners for purposes of applying Article 14 of the Treaty. Accordingly, A is treated as having a fixed base regularly available to him in the United States. A is subject to U.S. net income taxation on his allocable share of income from P to the extent that such income is attributable to the fixed base in the United States without regard to whether A performs services in the United States.

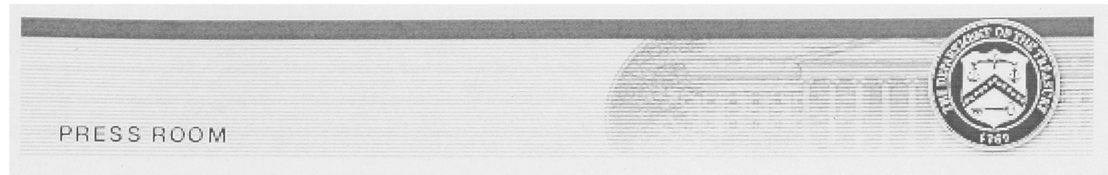
HOLDING

A is treated as having a fixed base regularly available to him in the United States and is subject to U.S. net income taxation on his allocable share of income from P to the extent that such income is attributable to P's fixed base in the United States, without regard to whether A

performs services in the United States. This holding also is applicable in interpreting other U.S. income tax treaties that contain provisions that are the same or similar to Article 14 of the Treaty.

DRAFTING INFORMATION

The principal author of this revenue ruling is Nina Chowdhry of the Office of Associate Chief Counsel (International). For further information regarding this revenue ruling, contact Nina Chowdhry on (202) 622-3880 (not a toll-free call).



FROM THE OFFICE OF PUBLIC AFFAIRS

January 28, 2004
js-1125

Treasury Names Robert Stein as Deputy Assistant Secretary for Macroeconomic Analysis

The Treasury Department today announced that Robert Stein was appointed this week as Deputy Assistant Secretary for Macroeconomic Analysis. He will be responsible for scrutinizing and reporting on current and prospective economic developments and assisting in the determination of appropriate economic policies. Mr. Stein originally joined the Treasury Department in January 2003 as a Senior Advisor in the Office of Economic Policy.

From January 2001 to January 2003 he was the chief economist for the Senate Budget Committee where he was responsible for evaluating the outlook for the U.S. economy, financial markets, and federal budget, analyzing key economic indicators and events, and estimating budget revenue and surpluses. Prior to the Senate Budget Committee, he was the staff director of the Senate Banking Subcommittee on Economic Policy (1999-2000). Before that he was on the staff of Congress's Joint Economic Committee as an economist, senior economist, and deputy chief economist (1996-1999).

He holds a B.A. in economics (with honors and distinction) from Georgetown University and a law degree from George Washington University.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 30, 2004
JS-1126

Statement of Secretary John Snow on the 2003 Fourth Quarter Gross Domestic Product Report

Today's report on GDP growth in the fourth quarter of last year further demonstrates that a good recovery is underway. Economic growth in the second half of 2003 was the fastest in nearly 20 years. The President's well-timed Jobs and Growth tax relief plan led to broad-based improvements. Following last year's exceptional third quarter, 2003 ended with solid gains. We are seeing good economic news on many fronts and we are encouraged, but we are not satisfied. The Administration's efforts will continue until every American looking for work can find a job.

-30-

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 30, 2004
JS-1127

MEDIA ADVISORY:
Department of the Treasury "Blue Book" Technical Tax Briefing

Treasury Assistant Secretary for Tax Policy Pam Olson will hold the "Blue Book" technical background briefing on the tax proposals in the President's FY 2005 budget on Monday, February 2, 2004 at 12:00 p.m. in room 4121 (Treasury's media room). This session will provide a synopsis of the tax proposals and will also allow for a Question and Answer session with Tax Policy staff. No cameras will be admitted-- this is a "pen and pad" only briefing.

Media without Treasury press credentials planning to attend should contact Treasury's Office of Public Affairs at (202) 622-2960 with the following information: name, social security number and date of birth. This information may also be faxed to (202) 622-1999.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 29, 2004
JS-1128

Remarks of Mark Sobel
Deputy Assistant Secretary
for
International Monetary and Financial Policy
at the Second Annual European Financial Services Conference
Brussels, Belgium
January 27, 2004

"The US-EU Financial Market Dialogue: The Transatlantic Dimension"

It is an honor to address the "Second Annual European Financial Services Conference." I thank the conference organizers for putting this event together and for recognizing that Europe's momentum on financial markets is extremely important to the United States.

The United States has strongly supported European integration for many decades. The United States and the European Union are the two largest economies in the world and share a special responsibility for promoting the sound management of the global economy. The policies pursued in the United States and Europe are critical not only for the citizens of each area, but also for the world at large.

A central aim of US foreign economic policy is to help promote strong global growth. The United States has been doing its part, and continues to do so. Other parts of the world are also growing. But in many key industrial countries, weaknesses persist, and the world has relied too long on the United States as a single motor.

Last September, the G-7 Finance Ministers committed to an Agenda for Growth. Under this Agenda, the G-7 will focus on "supply side" surveillance, benchmarking progress in implementing reforms to boost productivity in such areas as labor markets, pensions, and tax systems. To be sure, concrete actions are underway on these fronts. But further reforms are needed to create the flexibility for bolstering growth in and across our countries. The need for increased global growth will be a key discussion topic among G7 Finance Ministers this year.

US history teaches us that the creation of efficient and robust capital markets is critical for strong growth. The openness of the US financial system, its depth and liquidity, and fierce competition have been one of the most potent disciplinary forces for enhancing competitiveness, strengthening consumer choice and welfare, and offering borrowers capital at costs better suited to promoting investment.

Various studies have shown that Europe's Financial Services Action Program (the FSAP) has the potential to raise European growth by one percentage point per annum in a decade. Were this potential to be achieved, the FSAP -- building on the euro's successful launch, let alone other structural reforms -- could represent a lasting accomplishment for Europe and a win-win opportunity for Europe, the United States and the world.

The world is living through a period of rapid globalization in which financial markets are a key driver. The FSAP is not just about creating a unified European financial

market. It is about anchoring the European market in an integrated, state-of-the-art and open global financial marketplace. Needless to say, US financial institutions are leaders of the global financial industry and we have a strong interest in seeing that US firms are able to compete globally on fair terms, allowing their competitive and innovative energies to flow.

Indeed, US firms are a large, longstanding and dynamic part of the European financial market, and the Euromarkets in particular. They can help the evolution of the European market. For example, US financial institutions are leaders in mutual fund products, critical to the development of US pension plans. Most analysts cite the evolution of defined contribution systems as one of the keys for addressing European demographic challenges.

As the FSAP process moves forward, the United States also recognizes that the process of building a global financial market is a two-way street. European firms are understandably interested in access to US capital markets.

Also, Europe and the United States have different financial legal, historical and cultural traditions; we are not identical; and our actions may have "spillover" effects into the other's jurisdiction. I am reminded every day of this as outside my office in the Treasury hallway hangs a picture of former Secretary Carter Glass, one of the co-authors of the Glass-Steagall Act, who obviously was not a proponent of universal banking.

In achieving our common objectives, US and European authorities will face new challenges, particularly in balancing competitive efficiencies with sound regulation. Sound regulation is essential for investor protection and confidence. But the financial industry is always a step ahead of the regulators, and all would be ill served if regulation stifled innovation. Thus, regulators and supervisors should consult closely with financial institutions, understand how firms operate, and take their perspectives into account. To do so, regulations should be made in a transparent manner, open to public comment.

For these reasons, the US and EU have a strong interest in closely cooperating on financial markets. Almost two years ago, technical teams from both sides began meeting informally in the US-EU informal financial market dialogue. On the US side, technical officials consist of representatives from the US Treasury, the SEC, and the Federal Reserve. The Commission represents Europe. Since then, we have met roughly every four months. This dialogue was cited by President Bush and President Prodi at their Summit as a strong example of US-EU cooperation. In addition, the dialogue is supplemented by high-level policy meetings; the SEC is developing a regulatory dialogue with CESR; and PCAOB representatives have forged strong ties with Brussels.

The US Treasury has a broad interest in financial market issues. Regulatory agencies such as the SEC, Fed, OTS and PCAOB are independent and it is their job to protect a sound financial system at home. Thus, in the dialogue, we discuss issues that are emerging and the implications of these issues for each other; we seek to iron out legitimate issues; and when problems arise, we seek to work them out. In short, we manage "spillovers". How are we doing? How does the US see the dialogue?

The United States strongly welcomes the FSAP. We know that the FSAP timetable is ambitious. But even if there are slippages, setting ambitious deadlines and working on a fast track can be a virtue.

We are pleased by the more transparent European processes for rule-making that have developed in the last two years and the increased consultations with market participants. Our sense is that Brussels and the European Parliament now appreciate that working with market participants can improve European rule-making, create buy-in for proposed regulations, and strengthen European financial markets.

We are also watching many individual FSAP measures and other looming issues.

The Financial Conglomerates Directive has attracted considerable attention. It requires that foreign supervisory regimes be deemed "equivalent" by Europe for foreign-based firms to operate in Europe without costly legal and financial changes that could hurt the European market. We, of course, believe that the US system of supervision is top flight, world class and sound. But to help Europe reach a finding of equivalence, our regulators have worked closely with European regulators to deepen understanding of US practices. These discussions over two years have included a full explanation of the system of US regulation of investment banks, as well as Federal Reserve and OTS supervision. They have also led the SEC to issue a rule proposal formalizing the SEC's supervision of broker-dealers on a consolidated group-wide basis. A formal equivalence finding may be several months off, but the FCD is to be transposed into national laws by August 2004 and take effect in 2005. Time is short. Europe should dispel uncertainty and move rapidly to find equivalence.

The Council of Ministers has recently agreed upon an Investment Services Directive and the European Parliament is now following up. The directive could have profound implications for the liquidity of equity trading in Europe. The US has one of the most efficient equity markets in the world, and one in which "internalization" of transactions allowing for "price improvements" for larger customers has long been practiced, consistent with the principle of transparency. In managing spillovers through the dialogue, both Europe and the United States have emphasized the need to achieve our common objectives in substance -- the dialogue is about rewarding innovation and allowing regulation to support different market practices in a neutral manner. How internalization is permitted in the European context is extremely important for the future vibrance of European financial markets.

Europe is also moving forward with a Takeover Directive after many years of internal discussion. An integrated economic space for M&A activity throughout the Union which transcends national borders would represent forward movement for the integration of EU capital markets, further strengthen the competitiveness of Europe and the world economy and contribute vitally to the achievement of the FSAP's lofty growth objectives.

Large direct investment flows between the United States and Europe have taken place for centuries -- think of the building of our canals and railroads. This is an important achievement that has benefited our economies. The stock of European FDI in the US, at historic cost, is over $860 billion and some 64% of all FDI in the US; the US stock of FDI in Europe is over $700 billion and 46% of the stock of total US FDI. In recent years, we have witnessed eye-popping takeovers: Daimler has taken over Chrysler; Deutsche Bank has taken over Banker's Trust and Alec Brown; British Telcom bought Yellow Book USA; and Unilever bought Best Foods. As we in the United States sift through the complex legal provisions of the Takeover Directive, we believe it is essential that there be a clear statement that notions of reciprocity vis-à-vis third countries be avoided. Otherwise, there is risk of generating unnecessary uncertainty for potential investors in Europe, which would prove economically deleterious.

For decades, US firms have listed securities on the Euromarkets on the basis of US GAAP. But the implication of the Transparency and Prospectus Directives is that for all securities admitted to trading in European markets by 2005, the issuing firms will have to produce financial reports on the basis of IAS. Further, the Transparency Directive does not effectively provide for grandfathering of existing securities. US firms and institutions remain huge issuers in the Euromarkets. We understand that Europe is now looking at these issues and considering whether USGAAP should be found "equivalent" or "comparable" for the purposes of the Directives. In the meantime, third party issuers are facing a period of tremendous uncertainty. Already, some are reportedly pulling back from the Euromarkets. Clearly, were this business to diminish, the Euromarkets would be smaller and less liquid, and the cost of raising capital for those firms continuing to use the Euromarkets higher. Such an outcome would be inconsistent with the noble objectives and growth ambitions of the FSAP This issue should be tackled resolutely and expeditiously.

Over the medium term, we also recognize that the FSAP faces many more

challenges and that the European Commission and the member state Financial Services Committee are looking to the future. The presence of national clearing and settlement systems means that European cross-border transactions can cost 5 to 15 times higher than national costs. Reducing these costs would surely benefit European consumer welfare enormously. So would a reduction in impediments to cross-border pension fund activities. Corporate governance, enforcement and cross-border retail issues will also be important priorities.

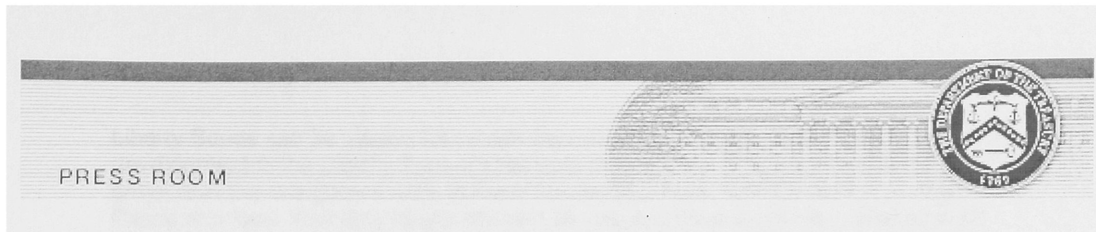
Tackling all of these issues, dispelling uncertainty and creating a liberal and integrated cross-border European space for financial markets will be critical if the true promise of the FSAP is to be secured. We wish Europe the best in achieving these justifiably lofty and ambitious goals and we will be monitoring implementation closely.

In the wake of Sarbanes-Oxley, the SEC thoroughly discussed with European officials such issues as auditor independence, loans to bank executives and directors, certification of financial statements by CEOs and CFOs, and standards related to audit committees. While the letter and spirit of Sarbanes-Oxley were fully observed, EU concerns were accommodated. Notwithstanding some hiccoughs following the advent of the Public Company Accounting Oversight Board (PCAOB), the PCAOB launched bilateral talks with Europe and a healthy dialogue is underway.

Adding to this agenda, the FASB and IASB are working to converge global accounting standards. US officials are mindful of the bigger picture. Converged accounting standards -- each consistently applied, implemented and enforced -- would make accounting in the US and Europe a similar exercise, accelerating momentum toward an even more dynamic transatlantic capital market. Recent events on both sides of the Atlantic have underscored that neither of us is infallible and that the issue is not whether GAAP or IAS is better or worse -- rather, the issue is how to find the right balance between rules and principles underlying these standards, how to ensure effective implementation of accounting standards, and how to best strengthen investor confidence.

On our side, the United States intends to continue its close cooperative relations with Europe for the good of the transatlantic financial market, for the good of US-European relations, and for the good of the global economy. In doing so, we intend to buttress our close ties with the Commission, to build further bridges to the European Parliament and to strengthen our outreach with the private sector and member states.

In the final analysis, the US-EU financial market dialogue and regulatory cooperation will be constructing a pillar of the international financial architecture of the 21st century. Progress is being made, but many challenges lie ahead. The United States will remain engaged.



FROM THE OFFICE OF PUBLIC AFFAIRS

January 30, 2004
JS-1129

Snow tells Pataki and Bloomberg that President's Budget seeks to extend Liberty Bonds

Secretary of the Treasury John W. Snow today spoke with New York Governor George Pataki and New York City Mayor Michael Bloomberg by phone to deliver the news that President Bush's FY 2005 budget request includes an extension of the New York Liberty Bonds program until 2009.

"New Yorkers have stood strong in the face of terrorists and have made great progress in their efforts to rebuild and recover. The President's request to extend the Liberty Bonds program for five more years will help make further revitalization a reality," said Secretary Snow.

New York Liberty Bonds were created as part of the economic stimulus package that President Bush signed in the wake of the terrorist attacks of September 11, 2001. The Liberty Bond program allows the State of New York and New York City to issue up to $8 billion in special tax-exempt private activity bonds to help finance capital projects in the newly-designated Liberty Zone, located in lower Manhattan.

Approximately $2 billion in Liberty Bonds have been issued or authorized to date. There is currently a backlog of applications for financing that may not have been processed by the program's original expiration date at the end of 2004.

Fact Sheet: New York Liberty Bonds

What are Liberty Bonds?

New York Liberty Bonds are special private activity bonds that can be used to finance capital projects primarily in the Liberty Zone, the area of Manhattan south of Canal Street, East Broadway and Grand Street. Interest on the bonds is exempt from federal income tax.

When was the Liberty Bond program created?

The Liberty Bond Program was part of the economic stimulus package that was signed by President Bush in the wake of September 11, 2001, attacks on the World Trade Center and the Pentagon. The program was established to help New York City rebuild and recover by spurring economic development in the areas hardest hit by the attacks.

How big is the program?

The economic stimulus package authorized up to $8 billion dollars in Liberty Bonds. At this point, New York has issued or authorized approximately $2 billion of these bonds. There are many pending applications that would not have been processed by the program's original expiration date at the end of 2004.

How can Liberty Bonds be used?

Liberty Bonds can be issued for certain housing, office, utility, and retail development in the Liberty Zone and surrounding areas. First priority is given to projects in the designated area in lower Manhattan. New York Governor George Pataki and New York City Mayor Michael Bloomberg have each been allocated $4 billion for the program. Up to $800 million of the $8 billion total may be issued for retail development, up to $1.6 billion for residential rental projects in the Liberty Zone, and up to $2 billion for commercial projects in New York City but outside the Liberty Zone.

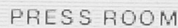
How do Liberty Bonds work?

Liberty Bonds are sold to private investors to provide capital for designated development projects. The bonds are not obligations of the State or City, but are instead obligations of the entities established by the State or City to issue the bonds. The bonds are secured by pledged project revenues, typically with no recourse to the issuer. Interest on the bonds is exempt from federal, State, and City income tax, and these savings are passed on to the borrower in the form of a lower interest rate. The interest rate available to a borrower under the New York Liberty Bond Program will depend on the individual project's credit worthiness and financing structure, as well as general market conditions.

The New York Liberty Development Corporation, a local development corporation formed at the direction of the Empire State Development Corporation, and the New York City Industrial Development Agency will issue bonds for commercial and utility projects. The State's issuer for residential facilities will be the New York State Housing Finance Agency; the City's residential issuer will be the New York City Housing Development Corporation.

Why does the program need to be extended?

New York City has come a long way in the last two years, but President Bush knows there is still more opportunity and potential in the Liberty Zone and surrounding areas. New York City has utilized approximately $2 billion of the $8 billion that was allocated to the program.
However, it has taken longer than expected for the City to be in a position to utilize the full potential for these bonds. Therefore, President Bush has proposed an extension in the program until 2009.



PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 30, 2004
JS-1130

Statement from Assistant Secretary of the Treasury for Financial Institutions Wayne A. Abernathy Warning About Recent Fraudulent E-Mail Schemes

Recently, many Americans have received a series of fraudulent e-mails which direct recipients to websites where they are asked to verify sensitive personal information. The e-mails claim that the individual's personal information is necessary to assist in the fight against terrorism or for some other purpose supposedly required by law. These e-mails are purportedly sent from several government agencies or include content related to government agencies including the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Securities Investor Protection Corporation and others. The websites to which the email recipients are directed are often very similar to, if not actual clones of official government sites.

The fraudulent e-mails are part of a scam known as "phishing." Phishing is the fraudulent scheme of sending an e-mail to a user falsely claiming to be a legitimate company. The email attempts to con the user into surrendering private information that could later be used for identity theft. The e-mail directs the user to visit a web-site where they are asked to update personal information, such as name, account and credit card numbers, passwords, social security numbers and other information. The Web site, however, is bogus and set up only to steal the user's information.

As part of the Treasury Department's efforts to fight identity theft, we want to assure Americans that federal financial agencies do not communicate with consumers by e-mail requesting important personal information such as your name, account numbers, date of birth, social security number.

Consumers can protect themselves from this latest identity theft scam by following these useful tips, which were developed by the Federal Trade Commission:
• If you get an email that warns you, with little or no notice, that an account of yours will be shut down unless you reconfirm your billing information, do not reply or click on the link in the email. Instead, contact the company cited in the email using a telephone number or Web site address you know to be genuine.
• Avoid emailing personal and financial information. Before submitting financial information through a Web site, look for the "lock" icon on the browser's status bar. It signals that your information is secure during transmission.
• Review credit card and bank account statements as soon as you receive them to determine whether there are any unauthorized charges. If your statement is late by more than a couple of days, call your credit card company or bank to confirm your billing address and account balances.
• Report suspicious activity to the FTC. Send the actual spam to uce@ftc.gov. If you believe you've been scammed, file your complaint at www.ftc.gov, and then visit the FTC's Identity Theft Web site (www.ftc.gov/idtheft) to learn how to minimize your risk of damage from identity theft.

The Treasury and federal financial regulators are working hard to combat identity theft including the use of new tools in legislation recently signed by President Bush. But all consumers must take reasonable precautions in the use of their personal

financial information in order to help prevent themselves from becoming victims of identity thieves.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 2, 2004
JS-1131

**The President's Savings Proposals:
Tax-Free Savings and Retirement Security
Opportunities for all Americans**

Today the Treasury Department announced that the President's FY 2005 Budget includes the following savings initiatives: ***Retirement Savings Accounts, Lifetime Savings Accounts, Employer Retirement Savings Accounts, and Individual Development Accounts***

The first proposal would create two consolidated savings accounts: ***Retirement Savings Accounts (RSAs) and Lifetime Savings Accounts*** (LSAs) that will allow everyone to contribute -- with no limitations based on age or income status. Individuals will be able to convert existing tax-preferred savings into these new accounts in order to consolidate and simplify their savings arrangements.

• RSA and LSA contribution limits will be $5,000 per year. This contribution limit is modified from last year's FY04 Budget proposal, which had a contribution limit of $7,500.

"Americans want a secure future: simplifying savings will help them reach that goal," stated Treasury Assistant Secretary for Tax Policy Pam Olson. "The savings options proposed today will give all Americans the opportunity and flexibility they need to save for their retirement security and other needs. The proposals make saving simple for everyone and for every purpose. They stress the importance of getting off the spending couch and into the savings gym."

The second proposal would create ***Employer Retirement Savings Accounts (ERSAs)*** to promote and simplify employer sponsored retirement plans. The proposal would consolidate 401(k), SIMPLE 401(k), 403(b), and 457 employer-based defined contribution accounts into a single type of plan more easily established by any employer.

• This proposal is modified from the previous FY04 Budget proposal to enhance flexibility and encourage small businesses to fund a custodial ERSA for their employees. Employers with 10 or fewer employees would be able to fund an ERSA by contributing to a custodial account, which is similar to a current-law IRA.

The third proposal would create ***Individual Development Accounts (IDAs)*** help lower-income individuals save. This proposal would provide dollar-for-dollar matching contributions of up to $500 targeted to lower income individuals. Matching contributions would be supported by a 100 percent credit to sponsoring financial institutions.

**The President's Proposal to Expand Tax-Free Savings
Description of Proposal**

RETIREMENT SAVINGS ACCOUNTS (RSA)

$5,000 annual contribution limit (indexed for inflation).
Available to all individuals – no income limits (contributions cannot exceed compensation), no age limits.
Contributions would be nondeductible (like Roth IRAs).
Earnings would accumulate tax-free, and qualified distributions would be excluded from gross income.
Qualified distributions could be made after age 58 or in the event of death or

disability.
- Nonqualified distributions: Distributions in excess of prior contributions would be included in income and subject to an additional tax.

Conversions to RSAs: Roth IRAs, Traditional and Nondeductible IRAs
- Roth IRAs would be renamed RSAs and benefit from the new rules for RSAs.
- Existing traditional and nondeductible IRAs could be converted into an RSA by taking the conversion amount into gross income, similar to a current-law Roth conversion.
- No income limit would apply to the ability to convert.
- Existing traditional and nondeductible IRAs that are not converted to RSAs could not accept any new contributions after 2004.
- New traditional IRAs could be created to accommodate rollovers from employer plans, but they could not accept any new individual contributions.
- Individuals wishing to roll an amount directly from an employer plan to an RSA could do so by taking the rollover amount (excluding basis) into gross income (i.e., "converting" the rollover, similar to a current law Roth conversion).
- Several of the withdrawal exceptions would be eliminated, increasing the likelihood that money set aside for retirement is there for retirement.

LIFETIME SAVINGS ACCOUNTS (LSA)
- $5,000 annual contribution limit (indexed for inflation).
- Available to all individuals – no income limits, no age limits.
- Contributions would be nondeductible (like Roth IRAs).
- Earnings would accumulate tax-free and all distributions would be excluded from gross income.
- No minimum required distribution rules would apply at any age throughout owner's life.
- Contribution limit of $5,000 applies to the individual owner of the account, not the contributor.
  - o Contributors could make annual contributions to the accounts of other individuals.
  - o Annual aggregate contributions to an individual's accounts could not exceed $5,000.

Consolidation to LSAs:
- Individuals could convert balances from Coverdell Education Savings Accounts (ESAs) or Qualified Tuition Plans (QTPs) to LSAs.
- Individuals could continue to contribute to ESAs and QTPs as under current law.
- Health Savings Accounts (HSAs) and Archer Medical Savings Accounts (MSAs) would be retained.

EMPLOYER RETIREMENT SAVINGS ACCOUNTS (ERSA)
One Retirement Plan: Employer Retirement Savings Accounts would combine the array of existing retirement plans into one simple uniform regime:
- o 401(k)
- o SIMPLE 401 (k)
- o 403 (b)
- o Governmental 457
- o SARSEPs
- o SIMPLE IRAs

Access: Available to all employers

Simplified Administrative Rules: The new plan would be much simpler for employers to administer, so employers who are not already sponsoring a plan, especially smaller employers without the resources for administering plans, will be more likely to offer a retirement savings program for their employees.

- A single nondiscrimination test would apply to ERSA contributions, as compared to the double test that currently applies to 401(k) plan contributions.

- Employers could avoid nondiscrimination testing altogether if they satisfy a simplified safe harbor.

- ERSAs sponsored by state and local governments and section 501(c)(3) organizations would not be subject to nondiscrimination testing under certain circumstances.

A simple custodial ERSA would be allowed for employers with 10 or fewer employees to help reduce costs to small businesses and encourage them to offer plans. The custodial ERSA would be similar to a current-law IRA. Employers would be exempt from annual reporting requirements and provided relief from most ERISA fiduciary rules similar to the relief provided to sponsors of SIMPLE IRAs.

The rules applicable to defined benefit plans would not be affected by this proposal.

INDIVIDUAL DEVELOPMENT ACCOUNTS (IDAs)
Individual Development Accounts would create accounts with dollar-for-dollar matching contributions targeted to lower income individuals.

- Dollar-for-dollar matching contributions provided to individuals up to $500.
- Single filers with incomes below $20,000, joint filers with incomes below $40,000 and head of household filers with incomes below $30,000 would be eligible.
- Matching contributions supported by 100 percent tax credit for sponsoring financial institutions that provide matches to individuals.
- A $50 per account credit for financial institutions to cover ongoing costs of maintaining and administering each account and providing financial education to participants.
- Qualified withdrawals of contributions and matching funds for higher education, first-time home purchase, and small business capitalization.

The President's Proposal to Expand Tax-Free Savings Important for the Future

Continues to Build an Ownership Society

• The United States is increasingly an ownership society. More than half of all households – 84 million individual investors – own stock directly or through stock mutual funds.

• The savings package further promotes an ownership society by:

o improving access by removing barriers to tax preferred saving.
o making savings simpler by reducing complexity and unifying the rules.
o improving fairness by providing the benefits of tax preferred savings to those least able to save for the very long-term.

• Through the savings package, taxpayers get the benefit of paying the tax man upfront, rather than when withdrawing funds for retirement or other needs. Taxpayers' receive the full return on investments giving them greater certainty about the amounts available for their retirement and other needs.

• A majority of taxpayers will be able to move all of their savings in a few short years into tax free savings accounts. This will allow taxpayers to avoid the complexities of reporting financial income on their tax returns and filing a schedule B and Schedule D.

• Increased education and financial literacy will help raise awareness of the importance of savings.
o Financial services firms will be more focused on counseling clients on maximizing financial security rather than the intricacies of the tax rules – adding value instead of paper work.

Enhances Low- and Moderate-Income Savings Opportunities

• The savings package simplifies individuals' savings decisions.
o Complex and confusing eligibility rules are replaced with one rule for both LSAs and RSAs: everyone can contribute.
o The special rules that dictate what qualifies as a penalty free withdrawal are replaced with one rule under LSAs: all distributions are tax-free.

• Tax preferred savings would become universally available.
o Individuals' saving will correspond more directly to their needs rather than to the

special uses prescribed by the tax laws.
o The availability of tax preferred savings opportunities to the low income under current law is largely illusory. The flexibility of LSAs allows access to tax preferred savings regardless of an individual's savings horizon and use.
o The current alphabet soup of accounts are available to low and moderate income taxpayers, but their shear complexity, for all practical purposes, closes them to low and moderate income taxpayers who don't have access to the sophisticated tax and financial advice needed to take advantage of them.
o Low-income individuals, in particular, may not have the resources to save for long into the future.
o Low-income individuals are the most likely to need their savings in an emergency, and the most likely to pay penalties for early withdrawal under current law.

• Uniform and simple rules will encourage financial services firms to market tax preferred savings more aggressively and to spend their resources on financial education and literacy.

• Dollar-for-dollar matching contributions up to $500 would be made available to lower income individuals through Individual Development Accounts (IDAs). The matching contributions would be supported by a tax credit to financial institutions.

Promotes Retirement Savings

• The ERSA proposal simplifies and unifies employer plan rules in a number of important ways. ERSAs will be much easier for employers to adopt and administer and will help reduce the costs to employers.

• ERSAs consolidate all types of employer plans into a single simplified plan.

• ERSA custodial accounts, available to employers with 10 or fewer employees, would be exempt from annual reporting requirements and provided relief from fiduciary rules.

• Lower administrative costs under ERSAs will translate into higher investment returns to employer plan participants, which will help encourage participation.

More uniform employer plan rules may lead to greater competition between financial services firms, which may further help drive down costs and increase returns to investors.

Encourages Savings and Promotes Economic Growth

• The package promotes savings in several ways.
o These proposals remove the current law penalty on saving. The after-tax return to savings is increased through greater access to tax preferred savings. Higher after-tax returns encourage savings.
o The simpler and more uniform rules for individual savings vehicles will encourage more savings.
o Lower costs for setting up and maintaining employer plans will increase returns and encourage additional savings.
o More uniform rules for employer plans will foster more competition for investor funds among financial services firms. More competition lowers costs and translates into higher returns to investors, further encouraging savings.

• Greater savings translates into more investment, greater capital accumulation, and higher living standards in the future.

• Greater savings means a more secure future for Americans of all income levels.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 2, 2004
JS-1132

**Preserving Cash Balance Plans for Workers:
Treasury Proposes Legislation to Protect Defined Benefit Plans and Ensure Fair
Treatment of Older Workers
in Cash Balance Conversions**

Today, the Treasury Department proposed legislation to ensure the fair treatment of older workers in cash balance conversions.

"This proposal will make sure that every company converting to a cash balance plan deals fairly with its older workers," said Secretary John Snow. "Cash balance plans play an important role in achieving retirement security for millions of American workers and their families. But we must make sure that companies changing from a traditional pension to a cash balance pension include a fair transition for older workers. Cash balance plans can be a better option, particularly for today's younger, more mobile workforce."

A cash balance plan is a pension plan that combines the benefit formula of a defined contribution plan with the worker investment security of a defined benefit plan. Cash balance plans are better suited to a mobile workforce because employees accrue more substantial benefits earlier in their careers and can take their cash balance benefits with them as they move from job to job. Under a cash balance plan, a hypothetical account is set up for each worker and is credited with hypothetical pay and interest credits. Most cash balance plans have been set up by "converting" traditional defined benefit plans.

Treasury's proposal would ensure fairness for older workers in cash balance conversions. The proposal would impose a 5-year "hold harmless" period after each conversion. During this period, the benefits earned by any worker under the cash balance plan would have to be at least as valuable as the benefits the worker would have earned under the traditional plan if the conversion had not occurred. The proposal would ban any "wear-away" of retirement benefits, so that all workers would earn benefits immediately after the conversion.

These protections would be enforced through a 100 percent excise tax. The tax would not apply if a company gives workers a choice between the traditional plan and the cash balance plan or if the cash balance conversion grandfathers current workers.

The proposal would also clarify that cash balance plans do not violate the age-discrimination rules that apply to pension plans as long as they treat older workers at least as well as younger workers. This would remove uncertainty created by inconsistent federal court decisions and would ensure the future of cash balance plans.

The proposal would also eliminate the "whipsaw" effect, which acts as a cap on the interest credits that cash balance plans can provide to workers. This would permit companies to give higher interest credits, allowing larger retirement accumulations for workers.

All changes would be effective prospectively from enactment of the proposal.

Attachments:
Cash Balance Plan FAQ

Cash Balance Plan Proposal

Frequently Asked Questions on Treasury's Proposal for Cash Balance Plans

What are the goals of the proposed legislation for cash balance plans?

The proposal would accomplish three major objectives. Specifically, the proposal would:

- Protect the defined benefit system by clarifying the status of cash balance plans.
- Ensure fairness for older workers in cash balance conversions.
- Remove the cap on interest credits in cash balance plans.

Together, these objectives will help strengthen the defined benefit system while ensuring that companies treat older and longer-service workers fairly when they convert to cash balance plans.

What is a cash balance plan?

A cash balance plan is a type of tax-qualified retirement plan. It is often described as a "hybrid" plan because it combines features of a defined benefit plan and a defined contribution plan.

A cash balance plan provides for annual "pay credits" to an employee's "hypothetical account" and "interest credits" on the balance in the hypothetical account. For example, a cash balance plan might provide for pay credits each year equal to 5 percent of compensation, with interest at the rate on long-term Treasury bonds.

The plan is a defined benefit plan, so the employer bears all investment risk and benefits are insured through the Pension Benefit Guaranty Corporation. Otherwise, the plan functions much like a defined contribution plan from the perspective of an employee.

The Pension Benefit Guaranty Corporation estimates that there are more than 7 million American workers covered by cash balance and other hybrid plans.

How does a cash balance plan differ from a traditional defined benefit plan?

A cash balance plan states the employee's benefit as an account balance, much like a 401(k) plan. A traditional defined benefit plan typically states the employee's benefit as an annuity payable at normal retirement age. The annuity is often expressed as a combination of a percentage of final average pay and years of service (for example, an annual annuity equal to 1 percent of final average pay times years of service).

A traditional plan delivers most of its value to an employee in the very last years before retirement. By contrast, a cash balance plan provides for more level accruals throughout an employee's working career.

Recent studies have shown that cash balance plans help employers compete in tight labor markets because of the more level accruals of cash balance plans. This is especially true where employers are trying to attract and retain more "mobile" workers. Studies have also suggested that cash balance plans may provide higher benefits for a majority of the next generation of workers than would traditional defined benefit plans.

So cash balance plans have an important role to play in the retirement security of millions of American workers and their families.

What is a cash balance conversion?

When an employer amends a traditional defined benefit plan to become a cash

balance plan, that process is known as a conversion. Most cash balance plans have been set up in this way.

Why is this legislative proposal needed?

Cash balance conversions can result in unfair treatment of older and longer-service workers because of the abrupt change from the traditional formula to a cash balance formula.

Many employers have voluntarily provided transition relief for older and longer-service workers. But ensuring the fair treatment of older and longer-service workers in conversions requires strengthening current law.

Current law does not protect the future expectations of older and longer-service employees affected by cash balance conversions, and it does not give Treasury the authority to impose fairness requirements for conversions. This very important issue has to be resolved through a change in the law.

What does the legislative proposal say about cash balance conversions?

The proposal requires that an employer converting to a cash balance plan provide for fair treatment of its older and longer-service workers. The proposal would do this in two ways.

First, the proposal would impose a 5-year "hold harmless" period after each conversion. During this period, the benefits earned by any employee under the cash balance plan would have to be at least as valuable as the benefits the employee would have earned under the traditional plan if there had been no conversion.

Second, the proposal would ban any wear-away of benefits at any time after the conversion. A wear-away occurs when an employee's benefits under the cash balance plan have to "catch up" with the benefits already accrued under the traditional plan. This means that some employees do not earn new benefits for a period after the conversion. By banning wear-away, the proposal would make sure that all employees immediately earn new benefits after the conversion.

Why is the "hold harmless" period 5 years?

The hold harmless period has to protect reasonable expectations of older and longer-service employees. At the same time, it cannot be so burdensome that the company decides to freeze the plan entirely, which harms all employees. A 5-year period strikes this balance.

Along with the complete ban on benefit wear-away, the 5-year period will ensure a fair transition for older and longer-service employees to the cash balance formula. In particular, employees who are within 5 years of normal or early retirement will have full protection under this proposal.

How would the new conversion rules be enforced?

The new conversion rules would be backed up by a 100 percent excise tax on the employer. The tax would apply to any shortfall between the benefits required under the new rules and the benefits actually provided by the cash balance plan. We believe that, faced with such an excise tax, employers will provide the benefits required under the proposal.

Some employers may convert to cash balance plans because they are experiencing adverse business conditions. For this reason, the amount of the excise tax would not exceed the greater of the plan's surplus assets at the time of the conversion or the plan sponsor's taxable income.

Would the excise tax apply if the employer provided some other kind of protection for its older and longer-service workers?

The excise tax would not apply if employees were given a choice between the traditional plan and the cash balance plan or if the conversion grandfathers current employees under the traditional plan. This would preserve flexibility of plan sponsors to implement other protections for older and longer-service employees.

Does this mean that Treasury thinks cash balance conversions violate the age-discrimination rules?

The legislative proposal released today goes beyond current law to ensure that every cash balance conversion provides for fair treatment of older and longer-service employees. In December 2002, Treasury and the IRS proposed regulations that interpret the current age-discrimination rules in the context of cash balance plans and cash balance conversions. Those regulations say that some, but not all, cash balance conversions could be age-discriminatory.

These new rules would apply even if the conversion satisfies the current age-discrimination rules.

Don't employers convert to cash balance plans mainly to save money on their pension obligations?

The evidence on the motivation for cash balance conversions is mixed. One recent study states that a majority of large companies had higher costs after a conversion while another suggests that costs were slightly reduced on average. Regardless, cost savings is only one of many possible motives for conversion. Even where an employer converts to save money, the conversion is preferable to simply freezing or terminating the plan, as long as older and longer-service workers are treated fairly.

What does the legislative proposal say about cash balance plans?

The proposal would clarify the legal status of cash balance plans under current law.

The federal courts have split on the question whether cash balance plans satisfy the age-discrimination rules. This has created uncertainty about the basic legality of these plans. Removing that uncertainty is critical to preserving the vitality of the defined benefit system, which provides retirement income security for millions of American workers and their families.

The proposal would clarify that a cash balance plan satisfies the age-discrimination rules if the plan provides pay credits for older and longer-service employees that are not less than the pay credits for younger employees and if the interest credits are not discriminatory.

The proposal would also clarify that certain transition strategies used in conversions do not violate the age-discrimination or other applicable rules. This would allow companies that convert to preserve the value of early retirement subsidies, for the benefit of employees, without violating the law.

The proposal would provide similar rules for other types of hybrid plans, such as pension equity plans.

Hasn't a federal court already said that cash balance plans are illegal?

One federal district court in Illinois said that one company's cash balance plan violates the age-discrimination rules (Cooper v. IBM Personal Pension Plan). However, other federal district courts have reached the opposite conclusion on other cash balance plans (Eaton v. Onan Corp.; Campbell v. BankBoston). These inconsistent decisions have left the law in a state of uncertainty.

So does this mean that Treasury thinks cash balance plans are good plans?

Treasury believes that cash balance plans have an important role to play in providing retirement security for millions of American workers and their families. However, Treasury also believes that the transition from a traditional defined benefit plan to a cash balance plan must provide for the fair treatment of older and longer-

service workers. That is why the proposal calls for new transition protections in cash balance conversions.

What does the legislative proposal say about "whipsaw"?

The proposal would eliminate whipsaw on a prospective basis.

This means that a cash balance plan could distribute an employee's account balance as a single sum as long as the plan does not credit interest at an above-market level. This would permit plan sponsors to give higher interest credits to employees, allowing larger retirement accumulations.

What exactly is whipsaw?

Whipsaw is an interpretation of current law, set out in IRS Notice 96-8, that says that cash balance plans must increase single sum distributions above employee account balances for future interest credits. This interpretation was never set out in formal IRS regulations. Nevertheless, three federal courts of appeals have followed the Notice 96-8 interpretation.

Whipsaw applies if the plan provides an interest crediting rate above the rate on 30-year Treasury bonds (or an equivalent rate).

So does that mean that the proposal will reduce employee distributions?

Absolutely not. The proposal would be effective on a prospective basis, so no employee would get a dollar less than what they would get without this new legislation.

In the future, the distributions of many employees should increase because the proposal will allow their employers to provide more generous interest credits, resulting in higher account balances and higher distributions.

What is the effective date of the proposal?

The entire proposal would be effective for periods after enactment. That means that the new rules will not apply before the date Congress enacts this proposal.

ENSURE FAIR TREATMENT OF OLDER WORKERS IN CASH BALANCE CONVERSIONS AND PROTECT DEFINED BENEFIT PLANS

Current Law

Qualified retirement plans consist of defined benefit plans, which allocate investment risk to the plan sponsor, and defined contribution plans, which allocate investment risk to plan participants. In recent years, many plan sponsors have adopted cash balance and other "hybrid" plans that combine features of defined benefit and defined contribution plans. A cash balance plan is a defined benefit plan that provides for annual "pay credits" to a participant's "hypothetical account" and "interest credits" on the balance in the hypothetical account. As with traditional defined benefit plans, the sponsor of a cash balance plan bears investment risk (as well as some mortality risk), and benefits are guaranteed by the Pension Benefit Guaranty Corporation. Otherwise, the cash balance plan functions like a defined contribution plan from the perspective of a participant.

Questions have been raised regarding whether and how cash balance plans satisfy the rules relating to age discrimination and the calculation of lump sum distributions.

Age Discrimination. Code section 411(b)(1)(H) provides that a defined benefit plan fails to satisfy the benefit-accrual rules if, under the plan, a participant's benefit accrual is ceased, or the rate of a participant's benefit accrual is reduced, because of the attainment of any age. Section 204(b)(1)(H) of the Employee Retirement Income Security Act of 1974 (ERISA) and section 4(i)(1)(A) of the Age

Discrimination in Employment Act (ADEA) set forth similar rules.

Age-discrimination questions have been raised regarding two aspects of cash balance plans. First, some have argued that pay credits for younger participants provide higher benefits than the same pay credits for older participants because the pay credits for younger participants accrue interest credits over longer periods. Although one federal district court has agreed with this analysis, others have rejected it. Compare Cooper v. IBM Personal Pension Plan, 274 F. Supp. 2d 1010 (S.D. Ill. 2003) (cash balance plan found age-discriminatory) with Campbell v. BankBoston, N.A., 206 F. Supp. 2d 70 (D. Mass. 2002) (cash balance plan found not age-discriminatory), aff'd, 327 F.3d 1 (1st Cir. 2003), and Eaton v. Onan Corp., 117 F. Supp. 2d 812 (S.D. Ind. 2000) (same).

Second, some have argued that "conversions" of traditional defined benefit plans to cash balance plans disadvantage older participants. A conversion occurs when a plan sponsor amends a traditional plan to make it a cash balance plan. A conversion can result in lower future accrual rates for some or all participants. If this occurs, ERISA section 204(h) and Code section 4980F require that participants receive advance notice. The conversion can also result in "wear-away" – a period following the conversion during which a participant's prior accrued benefits under the traditional plan exceed the benefits payable under the cash balance plan. Thus, during wear-away, the benefits under the cash balance formula of some or all participants must "catch up" with benefits accrued under the traditional plan. Wear-away may occur for the normal retirement benefit, the early retirement benefit, or both. However, under Code section 411(d)(6) and ERISA section 204(g), the conversion may not reduce the accrued normal or early retirement benefit of any participant.

Some have argued that the adverse effects of cash balance conversions fall more heavily on older participants than on younger participants because traditional plans usually provide more valuable accruals to older and longer-service participants. Many plan sponsors have adopted strategies to mitigate these effects, including protection of participant expectations through "choice" and "grandfathering" as well as avoidance of wear-away. However, these strategies have been voluntary, as current law generally gives the plan sponsor broad authority to amend a plan for any reason at any time. Hughes Aircraft Co. v. Jacobson, 525 U.S. 432, 443 (1999).

In December of 2002, Treasury and the IRS proposed regulations to address these and other age-discrimination issues. 67 Fed. Reg. 76123 (Dec. 11, 2002). The proposed regulations provide that a cash balance formula is not discriminatory as long as pay credits for older participants are equal to or greater than pay credits for younger participants. The proposed regulations also provide that cash balance conversions are not discriminatory as long as the conversions satisfy one of three permissible methods specified in the regulations. The proposed regulations do not prohibit reductions in future accrual rates or benefit wear-away because, under the conditions specified in the proposed regulations, those effects are not inherently age-discriminatory.

Calculation of Lump Sum Distributions. Three federal appellate courts have addressed the calculation of lump sum distributions under cash balance plans. Berger v. Xerox Corp. Retirement Income Guarantee Plan, 338 F.3d 755 (7th Cir. 2003); Esden v. Bank of Boston, 229 F.3d 154 (2d Cir. 2000), cert. dismissed, 531 U.S. 1061 (2001); Lyons v. Georgia-Pacific Salaried Employees Retirement Plan, 221 F.3d 1235 (11th Cir. 2000), cert. denied, 532 U.S. 967 (2001). All three courts held that a participant's hypothetical account balance must be projected to normal retirement age using the plan's interest crediting rate, converted to an annuity, and then discounted to a lump sum using the section 417(e) interest rate. If the plan's interest crediting rate is the section 417(e) rate, the present value of the normal retirement age annuity will be the same as the hypothetical account balance. However, if the plan's interest crediting rate is higher than the section 417(e) rate, the present value of the normal retirement age annuity – and the amount of any lump sum distribution – will be greater than the hypothetical account balance. This result is sometimes referred to as "whipsaw."

These federal court decisions have followed an analysis set out in IRS Notice 96-8. Many plan sponsors have responded to whipsaw by limiting the interest crediting rate to the section 417(e) rate (or a deemed equivalent). This response effectively makes the section 417(e) rate a ceiling on plan interest credits.

Reasons for Change

Although cash balance plans and cash balance conversions are not inherently age-discriminatory, current law does not provide adequate protection for older workers in every conversion. For example, the statutory age-discrimination rules do not prevent a plan sponsor from changing future benefit accruals. Also, current law does not prevent a plan sponsor from imposing wear-away of normal or early retirement benefits. (Current law actually restricts certain transition practices, such as preserving the value of early retirement subsidies through additions to participant account balances.) Many plan sponsors have voluntarily tried to mitigate any adverse effects that cash balance conversions may have on older and longer-service participants. However, ensuring the fair treatment of older and longer-service participants in conversions requires strengthening current law to guarantee reasonable transition protections and to prohibit benefit wear-away.

Inconsistent federal court decisions make it necessary to clarify that cash balance plans are not inherently discriminatory as long as older participants are treated at least as well as younger participants. Removing uncertainty about the basic legality of cash balance plans is critical to preserving the vitality of the defined benefit system, which provides retirement income security for millions of American workers and their families.

As applied by the courts, the whipsaw effect under Notice 96-8 has harmed participants by leading plan sponsors to limit interest credits to the section 417(e) rate. This results in lower retirement accumulations for participants. The whipsaw effect should be eliminated so that plan sponsors can give participants higher interest credits.

Proposal

The proposal would accomplish three major objectives:

1. Ensure fairness for older workers in cash balance conversions.

2. Protect the defined benefit system by clarifying the status of cash balance plans.

3. Remove the effective ceiling on interest credits in cash balance plans.

Ensure fairness for older workers in cash balance conversions. The proposal would provide new protections for participants in cash balance conversions that would ensure fair transitions from traditional plans to cash balance plans. For each of the first five years after a conversion, the benefits earned by any current participant under the cash balance plan would have to be at least as valuable as the benefits the participant would have earned under the traditional plan if the conversion had not occurred. Additionally, there could be no wear-away of normal or early retirement benefits for any current participant at any time.

To prohibit violations of the new transition protections, there would be a 100 percent excise tax, payable by the plan sponsor, on any difference between the benefits required under the proposal and the benefits actually provided by the cash balance plan. In recognition of the fact that some plan sponsors may be experiencing adverse business conditions, the amount of the excise tax could not exceed the greater of the plan's surplus assets at the time of the conversion or the plan sponsor's taxable income. Failure to implement the new transition protections would not result in disqualification of the plan.

The excise tax would not apply if participants were given a choice between the traditional formula and the cash balance formula or if the cash balance conversion grandfathered current participants under the traditional formula. This would preserve flexibility of plan sponsors to implement other provisions that protect older and longer-service participants.

Protect the defined benefit system by clarifying the status of cash balance plans. The proposal would clarify that a cash balance plan satisfies the age-discrimination rules if the plan provides pay credits for older participants that are not less than the pay credits for younger participants, in the same manner as any defined contribution plan. The proposal would also clarify that certain transition strategies

used in conversions (such as preserving the value of early retirement subsidies) do not violate the age-discrimination or other qualification rules. The proposal would provide similar rules for other types of hybrid plans and for conversions from traditional plans to other types of hybrid plans.

Remove the effective ceiling on interest credits in cash balance plans. The proposal would eliminate whipsaw, providing that a cash balance plan may distribute a participant's account balance as a lump sum distribution as long as the plan does not credit interest in excess of a market rate of return. The Secretary would be authorized to provide safe harbors for what constitutes a market rate of return and to prescribe appropriate conditions regarding the calculation of plan distributions. This would permit plan sponsors to give higher interest credits to participants, resulting in larger retirement accumulations.

Conforming amendments and effective date. There would be conforming amendments under ERISA and the ADEA for statutory changes to the existing age-discrimination and distribution rules (but not for the new excise tax).

All changes under the proposal would be effective prospectively. The legislative history would state that there would be no inference as to the status of cash balance plans or cash balance conversions under current law.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 2, 2004
JS-1133

Treasury Announces Market Financing Estimates

The Treasury Department announced today that it expects net borrowing of marketable debt to total $177 billion in the January – March 2004 quarter. The projected cash balance on March 31 is $20 billion. In the last quarterly announcement on November 3, 2003, Treasury announced that it expected net borrowing to total $160 billion with an end-of-quarter cash balance of $20 billion. This increase in borrowing is due to lower receipts, primarily from an increase in tax refunds, and higher outlays.

Treasury also announced that it expects net borrowing of marketable debt to total $75 billion in the April – June 2004 quarter. The projected cash balance on June 30 is $45 billion.

During the October – December 2003 quarter, Treasury's net marketable borrowing totaled $113 billion and the cash balance on December 31 was $33 billion. On November 3, Treasury announced that it expected net marketable borrowing to total $117 billion with an ending quarter cash balance of $35 billion. The decrease in borrowing is primarily attributable to lower outlays.

Additional financing details relating to Treasury's Quarterly Refunding will be released at 9:00 A.M. on Wednesday, February 4.

Related Documents:

- Supplemental Release: Treasury's Market Financing Estimates

SUPPLEMENTAL RELEASE: TREASURY'S MARKET FINANCING ESTIMATES

Today, the Treasury Department announced net borrowing of marketable debt for the January – March 2004 and April – June 2004 quarters.

Quarter	Estimated Borrowing ($ billion)	End-of-Quarter Cash Balance ($ billion)
Jan – Mar 2004	$177	$20
Apr – Jun 2004	$75	$45

Since 1997, the average forecast error in net market borrowing for the current quarter is $9 billion, of which $3 billion is attributable to differences in the end-of-quarter cash balance. Similarly, the average forecast error for the following quarter is $21 billion, of which $3 billion is attributable to differences in the end-of-quarter cash balance.

The following tables display and reconcile the variation between forecasted and actual net marketable borrowing in the October – December 2003 quarter.

Quarter	Estimated Borrowing ($ billions)	Actual Borrowing ($ billions)	Estimated End-of-Quarter Cash Balance ($ billions)	Actual End-of-Quarter Cash Balance ($ billions)
Oct – Dec 2003	$117	$113	$35	$33

Categories	? from Nov Estimate 1/
Receipts	$0
Outlays	+$7
Non-Marketable Activity	-$5
Change in Cash Balance	+$2
Decrease in Borrowing	+$4

1/ "+" and "-" represents the impact on financing needs. "+" represents a decrease in financing, while "-" represents an increase.

Additional financing details relating to Treasury's Quarterly Refunding will be released at 9:00 A.M. on Wednesday, February 5.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 2, 2004
JS-1134

**Acting Assistant Secretary of the Office of Economic Policy
Mark J. Warshawsky
Statement for the Treasury Borrowing Advisory Committee
of the Bond Market Association**

The economy continued to experience strong growth in the three months since the Committee's last meeting. While the pace of activity tapered from the unsustainably rapid rate of the third quarter, growth in real GDP in the fourth quarter was still very favorable at a 4.0 percent annual rate. That is well above the potential rate of growth of the economy, currently estimated by the Administration at 3.1 percent.

Real consumer spending continued to rise at a solid 2.6 percent annual rate in the fourth quarter even after growing at a 6.9 percent pace in the third quarter, the fastest pace in 17 years. Confidence is rising, with both the University of Michigan and Conference Board measures moving up in the fourth quarter to their highest levels in more than a year and surging further in January. Motor vehicle sales strengthened through the quarter and in December were at an annual rate of 17.9 million units, the second-highest monthly selling pace of the year. Gains in consumer spending are expected to be maintained this year as well, as jobs and incomes rise. In addition, last year's tax cuts are expected to continue to help lift the economy in the first half through higher refunds.

Households also continued to spend money on new homes, and the housing sector added more than 1 percentage point to real GDP growth in the third quarter and almost that much in the fourth. The number of housing starts surpassed an annual rate of 2 million in the final quarter of the year and 2003 marked the best year for homebuilding since 1978. The high level of housing starts at the end of last year implies another large contribution to growth from residential construction in the first quarter.

Business optimism has improved as well and that has translated into a strong upward track for investment. Corporate profits rose strongly in the third quarter and earnings reports for the fourth quarter have been very positive so far.

Roughly two-thirds of S&P 500 companies reported fourth-quarter results in January and almost 70 percent of those beat analysts' estimates. Equity prices have risen, with the S&P 500 increasing 26.4 percent last year after three straight years of decline. In addition, corporate interest rates have come down in tandem with the benchmark 10-year Treasury and yield spreads have narrowed.

Profit growth, low interest rates, and increased certainty that a sustained economic recovery is firmly underway, along with the investment-enhancing provisions of last year's stimulus legislation, have led to continued gains in business investment in equipment and software. That spending rose at a 10 percent annual rate in the fourth quarter, bringing growth over the four quarters of 2003 to almost 9 percent compared to an increase of just 1.6 percent over 2002. Additional gains are likely this year, with the consensus of private forecasters expecting about a 10 percent rise in business fixed investment for 2004 (as measured year/year).

Strong demand on the part of consumers and businesses has spurred manufacturers to boost production at a 6.6 percent annual rate in the fourth quarter, the largest increase in 3-1/2 years. Some of that production went into inventory rebuilding, as businesses began to restore depleted stocks in the fourth quarter after reducing them in the prior two quarters. Exports have started to turn around

and the economies of our major trading partners have strengthened a bit. After three quarterly declines, U.S. exports in real terms increased in the last two quarters of 2003.

Growth in profits and the consequent pickup in investment has been helped along by low unit labor costs, which have been held in check by exceptional productivity growth over the past few years. Since the fourth quarter of 2000 and through the third quarter of last year, productivity in the nonfarm business sector has surged at a 4.4 percent annual rate, the strongest performance of any comparable period in 40 years. High productivity growth contributed to low inflation, with consumer prices rising only 1.9 percent over the 12 months of 2003 and the core rate (excluding food and energy) up just 1.1 percent, the smallest increase since 1966. The low inflation environment has allowed the Federal Reserve to maintain an accommodative monetary policy stance, holding the target federal funds rate at 1.00 percent since the end of June.

Another favorable feature of current economic developments is an improving labor market, although job growth is not as strong as we would like. Labor markets began to turn around last summer, and the unemployment rate came down from 6.3 percent last June to 5.7 percent by the end of the year. Recent figures on initial claims for unemployment insurance benefits have been declining and are near a 3-year low, and surveys of business hiring have turned positive, such as those from the National Federation of Independent Business, the National Association For Business Economics, and the ISM for both manufacturing and non-manufacturing.

In the last five months of 2003 the economy created 278,000 nonfarm payroll jobs compared to a loss of 6,000 in the same period a year earlier. While the latest job gains were modest, employment is on an upward path.

The Administration projects further economic expansion and job growth this year and in the years ahead. Real GDP is forecast to grow 4.4 percent on an annual basis in 2004, building on the forward momentum of the second half of 2003. The unemployment rate is forecast to recede from the 5.9 percent average in the fourth quarter of 2003 to 5.5 percent in the fourth quarter of this year. Over the following five years of the forecast horizon, real GDP growth tapers to its potential rate of 3.1 percent and the unemployment rate levels off at 5.1 percent, in line with the consensus of private forecasters.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 2, 2004
JS-1135

Proposed Treasury Budget for FY 2005

The Department of the Treasury's FY 2005 budget reflects the President's commitment to strengthening the economy, fighting the financial war on terrorism and ensuring compliance with the tax laws.

The overall proposed budget for Treasury is $11.680 billion, a 4.5 percent increase over the current FY 2004 level appropriated, providing for the Department to continue in its vital role as the federal government's economic policymaker, financial manager and revenue collector.

Among the Department's key priorities are making the tax cuts permanent, improving tax compliance while ensuring that we maintain a fair tax system, using new technology to modernize the tax system, fighting the financial war on terror and safeguarding the government's finances, as well as the nation's financial systems and currency.

Making the Tax Cuts Permanent. The President's three tax relief measures have resulted in significant reduction in tax burdens for millions of American families and businesses. By making this relief permanent we will reduce uncertainty and continue to stimulate economic growth and job creation, benefiting millions of Americans.

Ensuring the Tax System is Fair - Maintaining World Class Service and Compliance with Tax Laws. A series of legislative proposals included in the budget are designed to close loopholes, halt several abusive tax avoidance transactions, and simplify the tax code. The budget reflects the Administration's continuing commitment to ensuring that all taxpayers pay their fair share of taxes, while reducing the needless cost borne by those attempting to comply. In addition, the budget provides for increases to the IRS' budget to enhance compliance.

Modernizing the Nation's Tax Systems through Technology Investments. The budget provides for the IRS to continue its efforts to replace current business systems and technology, which will allow for greater management focus and capacity on critical projects and initiatives as well as improvements to management and business processes.

Fighting the Financial War on Terror. As a vital part of the government's war on terror, Treasury offices work to disrupt and dismantle the financial infrastructure of terrorists, drug traffickers and other criminals and execute the nation's financial sanctions policies. The importance of these efforts is reflected in a 12.7 percent increase for the Financial Crimes Enforcement Network (FinCEN) and a 3.6 percent increase for Treasury's Office of Foreign Assets Control (OFAC) to strengthen our hand in the financial war on terror and other efforts against financial crime. The work of these agencies includes a concerted effort to safeguard financial systems through the longer term establishment of effective anti-money laundering strategies and programs.

Safeguarding the Government's Finances and our Nation's Financial Systems. The budget continues support for critical Treasury objectives such as increasing the reliability of the U.S. financial system, managing the federal debt effectively and efficiently, ensuring accurate and on-time payments and collections, effectively administering the government's financial systems and increasing economic security.

These are merely a few of the important priorities included in the President's budget for the Treasury Department. In delivering on these and other commitments, Treasury continues in its dedication to the President's Management Agenda and the Department's performance budgeting processes to align funding with performance and results.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 2, 2004
JS-1136

Remarks of Greg Zerzan, Deputy Assistant Secretary for Financial Institutions

Before the Council of Federal Home Loan Banks
Lake Buena Vista, Florida
February 2, 2004

Thank you very much for inviting me to join you today. It is always a great pleasure to spend time with men and women dedicated to improving the lives and communities of our fellow citizens, and I am grateful to you for asking me to participate in this event.

The past year has been one of tremendous progress for our country and our economy. I don't think I need to remind anyone in this room of the serious challenges that faced us at the dawn of 2003. The economy was still recovering from the terrorist attacks of 9/11, the burst of the market bubble and the corporate scandals of the previous two years. The recession inherited by the Bush Administration had taken a large toll, depressing profits and forcing Americans out of work. The President was determined to confront these crises directly.

When it came to dealing with the recession, the President was guided by one clear and central principal: in order to encourage economic growth, the government's job is to let people keep and spend more of their own money. In order to accomplish this, the President promoted successive rounds of tax cuts despite the strong opposition of some, who seemed reflexively opposed to putting money back in the hands of those who earned it. Under the President's plan-

• 109 million Americans have received, on average, a tax cut of $1,126.
• 23 million small business owners have received tax cuts averaging $2,209.
• Married tax payers, taxpayers with children, and in fact every American that pays taxes has seen reductions in their tax obligations.
• Businesses, and especially small businesses, have received new incentives to invest in plants and equipments and create new jobs.

The results of these tax cuts have been dramatic. We have emerged from the recession with an economy stronger and more resilient than many would have thought possible. New housing starts, business investment, corporate profits, and GDP have all increased. In the third quarter of 2003 alone, 328,000 new jobs were created.

In fact, our research at the Treasury Department informs us that, without these tax cuts, there would be 2 million fewer jobs in America than exist today under the President's plan. The economy has not simply endured the shocks of the last several years; it has overcome them.

We have also responded vigorously to the corporate scandals of the preceding years. New laws, such as the Sarbanes-Oxley Act, as well as vigorous prosecution of corporate wrongdoing, have ensured investors that their profits and losses will be based on real-world economic results, and not the misdeeds of a handful of irresponsible corporate executives. The performance of the stock market over the last year tells us that investor confidence has returned, and America's markets will remain the safest and most reliable investment opportunity in the world.

We also cannot forget the ongoing threat of terror that continues to plague not only our country, but all societies that favor democracy and the rule of law to tyranny and oppression. Let no one doubt that the world is a safer place thanks to the overthrow of the Al Qaeda and Taliban government in Afghanistan, and the recent

capture of Saddam Hussein. Although the war on terror continues, there is no doubt that the enemies of America sleep less and less comfortably every night, knowing that American justice is their fate.

With all the progress we have made in the last year, their remains work to be done. One of the areas of supreme importance to this Administration is continuing to make America a place where families have the opportunity to purchase their own homes. In order to promote home ownership, the President has called for increasing minority home ownership by 5.5 million families by the end of the decade. Remarkably, in the past 18 months alone 1 million minority families have already achieved their dream of owning their own homes.

America remains the best place in the world for a young family, just starting out, to buy a house. As you are well aware, the Treasury has called for the housing GSEs to register their equity securities with the Securities and Exchange Commission under the '34 Act. In order to help further the goal of ensuring Americans can obtain the dream of home ownership, the Administration has called for reforming the regulation of the housing government sponsored enterprises (GSEs).

The central principle behind reforming regulation of the housing GSEs is simple: these entities are world-class financial institutions, and they deserve a world-class regulator – one that is on par with other such financial institution regulators in the U.S. and around the world. The Administration has called for placing Fannie Mae, Freddie Mac and the Home Loan Banks under a single regulator equipped with the stature and the tools to ensure these institutions continue to operate in a safe and sound manner, and able to perform their mission of expanding home ownership opportunities for all Americans.

Last summer I was asked to head-up a survey of the Federal Home Loan Bank System, with particular view to the changes that have taken place in the System since passage of the Gramm-Leach-Bliley Act, and how the Banks' activities have evolved in recent years. In the course of this project, we have spoken with participants in the System, the Finance Board, most of the Banks, and others. We also solicited comments from each of the Banks individually, to which most have responded. As it relates to changes in the System since the passage of the Gramm-Leach-Bliley Act, our review has focused primarily on the implementation and results of the Act's new capital structure for the Banks, and on the Act's provisions that expanded access to the System for small depository institutions.

Any review of the activities of the Federal Home Loan Banks over the last 15 years reinforces our belief that the Bank System needs to be included in the new regulatory structure which has been proposed for the GSEs. The activities of the FHLBanks have been transformed to some degree from being focused solely on providing collateralized advances to members, to operating more active investment portfolios, including investments in mortgage-backed securities and more recently direct investments in mortgages from the Banks' mortgage purchase programs. As the risks undertaken by the housing GSEs have converged, there becomes a greater need that they be regulated in a similar manner.

By combining the housing GSEs under a single, credible regulator, we can ensure that the mission of promoting home ownership in our communities is conducted in a safe and sound manner, with a unitary view towards what's best for the housing finance system as a whole. The new regulator must be empowered with the ability to take a comprehensive look not only at each GSE individually, but also monitor developments in the housing finance market and the GSEs' operations in relation to it. The new regulator must have the power to review the new activities of a GSE, set prudent minimum and risk-based capital standards, and take prompt corrective action when necessary. The new regulator must also have the ability to conduct an orderly wind-down of an institution in the unlikely event that such an institution were to fail. These changes are not simply commonsense proposals to give the housing GSE regulator the same powers as our other financial regulatory agencies; they are proposals which will strengthen the GSEs and allow them to continue their important mission of increasing home ownership affordability for working Americans.

Finally, let me conclude with the message that I hope you all take from my remarks here today. When it was announced that Treasury was conducting a survey of the Bank System, and that the Administration was pursuing comprehensive regulatory reform of the GSE regulatory model, I sensed that there was genuine concern in the

System as to our ultimate goal. Please allow me to be clear: the Administration fully supports a strong, safe and sound Federal Home Loan Bank System. The changes we are proposing are intended to make sure that all of the housing GSEs can continue to serve the mission for which they were created. A credible regulator, equipped with the tools, power and stature to ensure the GSEs continue to focus on that mission, is in the best interest of the housing finance system, the Federal Home Loan Banks, and all Americans.

I thank you for inviting me to speak with you today, and I thank you for the work you do to expand home ownership affordability in our communities. As the reform process moves forward, your continued input is not only necessary, it is welcome. Thank you.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 4, 2004
JS-1137

Acting Undersecretary for Domestic Finance Brian C. Roseboro
February 2004 Quarterly Refunding Statement

We are offering, in this refunding, $56.0 billion of notes to refund approximately $26.6 billion of privately held notes and bonds maturing on February 15, raising approximately $29.4 billion. The securities are:

1. A new 3-year note in the amount of $24 billion, maturing February 15, 2007.
2. A new 5-year note in the amount of $16 billion, maturing February 15, 2009
3. A new 10-year note in the amount of $16 billion, maturing February 15, 2014.

These securities will be auctioned on a yield basis at 1:00 PM Eastern time on Tuesday, February 10, Wednesday, February 11, and Thursday, February 12, respectively. The balance of our financing requirements will be met through the monthly issuance of 2 – year and 5-year notes, the 10-year note reopening and 10-year TIPS, and bill offerings. The Treasury is likely to issue cash management bills in early March and April.

Expanding the TIPS Market

Treasury continues to examine ways of promoting inflation-indexed securities and expanding the market for this asset class. We are pleased with the growth and development of this market to date and remain committed to further expansion.

Treasury is considering the possibility of adding one or more TIPS maturity point(s), including maturities both longer than and shorter than the current 10-year TIPS. Additional issuance would help meet the natural and growing demand for inflation protected investments, expanding and diversifying demand for Treasury securities. Depending on the fiscal environment, expansion of the TIPS market could come from shifting existing longer-term nominal issuance to TIPS issuance.

A decision will be reached by the May 2004 refunding. We invite market participants to comment on this matter at the debt.managment@do.treas.gov.

Six-decimal price awards in Treasury auctions

Treasury currently computes price awards in auctions to three decimal places based on the 3-decimal stop-out yield of bank-discount rates tendered in auctions. On short-dated instruments, this practice can produce different yields that generate the same invoice price. In other words, there is not a 1-to-1 mapping between 3-decimal yields and 3-decimal prices.

Therefore, we will publish awarded price determined to 6-decimal places per hundred; this will permit price determinacy for all Treasury auctions and will result in settlement (purchase) prices to the exact penny for a $1,000,000 face amount. We will keep market participants informed about the status of this pending change, which we expect to implement in the second half of this year.

Auction Contingencies

Treasury has discussed the factors and circumstances that might lead to an auction delay with market participants. These discussions have made it clear that each potential disruption will be unique and the appropriate responses do not lend themselves to simple protocols. Nonetheless, two general operating principles evolved from the contingency discussions; first, preparedness is an area of continuous improvement requiring regular testing of contingency systems. Second, market uncertainty in the event of an auction disruption can be reduced through open and frequent communications with market participants.

As such, Treasury will conduct any announced auction that is disrupted within an hour of the originally scheduled time and in the event that circumstances and conditions are such that a one hour postponement cannot be met, Treasury will communicate information to market participants as it becomes available.

The next quarterly refunding announcement will take place on Wednesday, May 5, 2004.

Please send comments and suggestions on these subjects or others relating to debt management to debt.management@do.treas.gov.

Related Documents:

- Q1 Tables
- Q2 Tables

US TREASURY FINANCING SCHEDULE FOR 1ST QUARTER 2004
BILLIONS OF DOLLARS

ISSUE	ANNOUNCEMENT DATE	AUCTION DATE	SETTLEMENT DATE	OFFERED AMOUNT 4-WK	OFFERED AMOUNT 3-MO	OFFERED AMOUNT 6-MO	MATURING AMOUNT	NEW MONEY
4-WEEK AND 3&6 MONTH BILLS	12/24	12/29	1/2	12.00 A	16.00 A	15.00 A	51.00	-8.00
	12/31	1/5	1/8	9.00 A	17.00 A	16.00 A	45.00	-3.00
	1/8	1/12	1/15	8.00 A	17.00 A	16.00 A	44.00	-3.00
	1/15	1/20	1/22	9.00 A	18.00 A	16.00 A	46.00	-3.00
	1/22	1/26	1/29	14.00 A	18.00 A	16.00 A	46.00	2.00
	1/29	2/2	2/5	19.00 A	19.00 A	17.00 A	43.00	12.00
	2/5	2/9	2/12	20.00	19.00	18.00	40.00	17.00
	2/12	2/16	2/19	22.00	19.00	20.00	41.00	20.00
	2/19	2/23	2/26	24.00	19.00	20.00	46.00	17.00
	2/26	3/1	3/4	25.00	19.00	20.00	51.00	13.00
	3/4	3/8	3/11	25.00	19.00	20.00	51.00	13.00
	3/11	3/15	3/18	22.00	18.00	18.00	51.00	7.00
	3/18	3/22	3/25	18.00	18.00	18.00	54.00	0.00
					693.00		609.00	84.00
CASH MANAGEMENT BILLS								
13-Day Bill	12/29 Matures 1/15	12/30	1/2		15.00		15.00	0.00
11-Day Bill	3/2 Matures 3/15	3/3	3/4		20.00		20.00	0.00
COUPONS						CHANGE IN SIZE		
5-Year Note	1/5	1/7	1/15		16.00 A		15.22	0.78
10-Year TIPS	1/5	1/8	1/15		12.00 A	+ 1.00		12.00
2-Year Note	1/26	1/29	2/2		26.00 A		24.55	1.45
3-Year Note	2/4	2/10	2/17		24.00			24.00
5-Year Note	2/4	2/11	2/17		16.00			16.00
10-Year Note	2/4	2/12	2/17		17.00		11.82	5.18
2-Year Note	2/23	2/25	3/1		26.00		23.74	2.26
5-Year Note	3/8	3/15	3/17		16.00			16.00
10-Year Note (R)	3/8	3/15	3/22		13.00			13.00
2-Year Note	3/22	3/24	3/31		27.00	1.00	24.54	2.46
					193.00		99.87	93.13

R = Reopening
A = Announced

Treasury announced a Q1 borrowing need of $177 billion on 2/2/04

NET CASH RAISED THIS QUARTER: 177.13

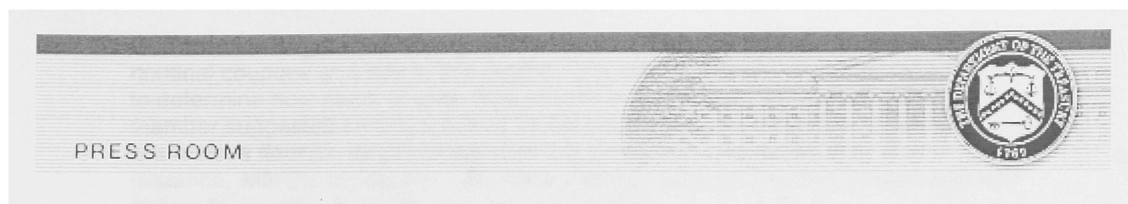
US TREASURY FINANCING SCHEDULE FOR 2ND QUARTER 2004
BILLIONS OF DOLLARS

ISSUE	ANNOUNCEMENT DATE	AUCTION DATE	SETTLEMENT DATE	OFFERED AMOUNT 4-WK	OFFERED AMOUNT 3-MO	OFFERED AMOUNT 6-MO	MATURING AMOUNT	NEW MONEY
4-WEEK AND 3&6 MONTH BILLS	3/25	3/29	4/1	18.00	18.00	16.00	57.00	-5.00
	4/1	4/5	4/8	18.00	18.00	16.00	58.00	-6.00
	4/9	4/12	4/15	16.00	18.00	16.00	56.00	-6.00
	4/16	4/20	4/22	13.00	18.00	16.00	53.00	-6.00
	4/23	4/26	4/29	11.00	17.00	16.00	53.00	-9.00
	4/30	5/3	5/6	8.00	17.00	16.00	54.00	-13.00
	5/7	5/10	5/13	8.00	16.00	16.00	51.00	-11.00
	5/14	5/17	5/20	20.00	16.00	16.00	48.00	4.00
	5/21	5/24	5/27	23.00	16.00	16.00	46.00	9.00
	5/28	5/31	6/3	20.00	18.00	16.00	43.00	11.00
	6/4	6/7	6/10	20.00	18.00	16.00	43.00	11.00
	6/11	6/14	6/17	16.00	17.00	17.00	52.00	-2.00
	6/18	6/21	6/24	15.00	17.00	17.00	55.00	-6.00
					640.00		669.00	-29.00
CASH MANAGEMENT BILLS								
10-Day Bill	4/1 Matures 4/15	4/2	4/5		20.00		20.00	0.00
9-Day Bill	5/3 Matures 5/14	5/4	5/5		15.00		15.00	0.00
11-Day Bill	6/2 Matures 6/15	6/3	6/4		20.00		20.00	0.00
COUPONS						CHANGE IN SIZE		
5-Year Note	4/5	4/6	4/15		16.00			16.00
10-year TIPS (R)	4/5	4/7	4/15		8.00	8.00		8.00
20-year TIPS	4/5	4/8	4/15		12.00	12.00		12.00
2-Year Note	4/26	4/28	5/3		27.00		24.32	2.68
3-Year Note	5/3	5/11	5/17		26.00	2.00		26.00
5-Year Note	5/3	5/12	5/17		18.00	2.00	16.21	1.80
10-Year Note	5/3	5/13	5/17		19.00	2.00	16.82	2.18
2-Year Note	5/24	5/26	6/1		28.00	1.00	27.00	1.00
5-Year Note	6/7	6/9	6/15		18.00			18.00
10-Year Note (R)	6/7	6/10	6/15		15.00	2.00		15.00
2-Year Note	6/23	6/28	6/30		28.00		26.52	1.48
					215.00		110.87	104.13

R = Reopening
A = Announced

Treasury announced a Q2 borrowing need of $75 billion on 2/2/04

NET CASH RAISED THIS QUARTER: 75.13



FROM THE OFFICE OF PUBLIC AFFAIRS

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February 4, 2004
JS-1138

Minutes Of The Meeting Of The
Treasury Borrowing Advisory Committee
Of The Bond Market Association
February 3, 2004

The Committee convened in closed session at the Hay-Adams Hotel at 11:35 a.m. The following members of the Committee were not present: Thomas Marsico and Richard Davis. Deputy Assistant Secretary for Federal Finance Timothy Bitsberger welcomed the Committee.

The Committee first discussed the sensitivity of Treasury's financing needs due to macroeconomic variables including GDP, inflation and interest rates, the first issue on the Committee's charge (attached). Mr. Bitsberger presented charts (attached) that depicted the long-run deficit projections of the Office of Management and Budget (OMB) and Treasury's residual financing needs based on these projections. Mr. Bitsberger pointed out that Treasury is well positioned to meet its borrowing needs with its current issuance calendar if OMB's deficit forecasts are met. Mr. Bitsberger also presented several charts showing the impact of changes in real GDP growth, inflation and interest rates on deficits as estimated by the OMB. One chart highlighted the projected increase in deficits in the out years from both a 1% decrease in real GDP growth in 2004 and a 1% decrease in real GDP growth every year through 2009. A second chart showed the impact on the projected deficit of a 1% increase in inflation and interest rates. One member observed that over the 5 year horizon, inflation has a greater absolute impact on the projected deficit.

One member noted that GDP growth is critical in determining deficits and Treasury's longer term financing needs, but that there was a lot of uncertainty over the next six to nine months. This generated discussion about tax refunds in the current fiscal year, with one member asking if the models depicted in the charts accounted for uncertainties such as spending that was announced but not implemented and the level of tax refunds this year. One member asked whether the risks Treasury faces are asymmetrical, while another member argued that they are symmetrical. One member suggested that Treasury, at a later time, give a presentation that better defines the explanatory variables discussed in the previous charts and their statistical impact. Mr. Bitsberger asked the Committee to discuss what further work Treasury should be undertaking to define and analyze some of the risks already discussed. In general, the Committee agreed with Mr. Bitsberger's statement that Treasury's issuance calendar is sufficient to meet the government's forecasted borrowing needs. One member commented that maximum flexibility was necessary and that the current calendar provided such flexibility.

The Committee next turned to the second question on the charge dealing with what criteria Treasury should use to assess its overall portfolio, balancing short and long-term issuance as well as nominal and Treasury inflation-protected securities (TIPS) issuance. Before the Committee discussed the issue, Mr. Bitsberger presented charts showing Treasury's percentage breakdown of annual issuance across maturities and distribution of marketable debt. Mr. Bitsberger also presented a chart showing that a small amount of long-term debt as a percent of total issuance can result in a larger percentage of the total portfolio held in long-term debt. Several members discussed the point that setting TIPS as a fixed percentage of the portfolio (either in nominal terms or as a percent of issuance) could be inflexible.

One member suggested looking at cash flows, noting the difference between TIPS, nominal coupons and bills in this regard. One way to look at the portfolio would be to determine how much of each type of cash flow Treasury would want. One member suggested setting a ceiling on bill issuance as a percentage of annual issuance, a floor for issuance between 2-3 years, and a target for long-term issuance, with the residual in TIPS. One member asked if Treasury should also look at how to manage its assets and not just liabilities.

Mr. Bitsberger then presented several charts showing demand for TIPS, highlighting some of the different investor demand at auction between TIPS and nominal securities and increasing demand from public pension funds. The Committee agreed that there is a growing demand for TIPS as a separate asset class. However, several members cautioned against overstating the point that the distribution of TIPS auction awards demonstrated a unique demand for the product. They noted that because TIPS are less liquid, investors who want to own them must buy at auction rather than in the secondary market, and that the auction data may show market segmentation, with investors buying nominal securities for liquidity purposes and TIPS for investment purposes.

Mr. Bitsberger then presented a chart showing the sensitivity of the real value of longer-term liabilities to changes in inflation. The chart highlighted that TIPS reduce the potential variability of the real value of Treasury's debt liabilities. The discussion then turned back to the question of what criteria Treasury should use to assess its overall portfolio. One member expressed concern that Treasury was not taking the level of interest rates into account when thinking about this issue. Another member noted that in thinking about issuing more TIPS, Treasury is correctly trying to identify new demand and take advantage of that demand and broaden the investor base. Another member reiterated that flexibility is an important criteria for Treasury.

Mr. Bitsberger asked the Committee where Treasury should decrease issuance if they introduce a new TIPS maturity point, assuming borrowing is held at its current level. The Committee was somewhat divided on the response. One member suggested that Treasury should first look at the reasons for a smaller-than-expected deficit, and that the first place to reduce issuance would be in the bill sector if the reasons are of a more temporary nature. Several members agreed with this assessment and one member recommended Treasury do more analysis comparing the cost of bill issuance versus TIPS issuance. However, other members thought that the first place to reduce issuance would be in the 10- or 5-year sectors of the nominal curve. One member sighted the decrease in flexibility if Treasury adds a 20-year TIPS, and suggested that it would be logical to cut back on longer-dated nominal issuance which is also more inflexible for Treasury. Another member thought that Treasury should place some importance on the level of interest rates when determining the best sector in which to reduce issuance.

The Committee then discussed the third question on the charge dealing with the November refunding calendar and auction schedule, which is complicated by several potential market-moving events and a holiday. Mr. Bitsberger presented three options for the refunding auction schedule. The Committee said they would take the options under consideration, and would look into possibly changing the scheduled meeting date for the Committee in November.

The meeting adjourned at 1:03 p.m.

The committee reconvened at 3:05 p.m. and finalized its recommendation for borrowing in this quarter and the April June quarter. Those charts are attached.

The committee made a presentation on Foreign Central bank purchases of Treasury securities.

First, Barry Kasman of JP Morgan made a presentation that macro economic conditions in both Asia and the US over the last several years resulted in a situation were the Asian governments have attempted to devalue their currencies and the Federal reserve has been on hold. This low US rate, low Asian currency relationship was good policy and beneficial to the economies in both regions for a

period of time. There are perceptions that it can continue indefinitely. However, economic fundamentals are changing with both Asia and the US experiencing growth and government policies of keeping US rates low and Asian currencies weak are artificial and do not match current macro economic conditions. Mr. Kasman estimates that foreign central bank purchases are actually depressing yields in the 2 to 3 year note sector by 60 to 80 basis points. He argues that the longer these policy positions ignore the macroeconomic fundamentals, the greater and potentially more disruptive a return to equilibrium will be. He saw 3 catalysts for such a disruption. These include the potential of Asian governments to control currency appreciation despite significant intervention activity, inflation in the US economy, and a pandemic such as SARS or avian flu through-out Asia.

Next, economist Mickey Levy of Bank of America made a presentation suggesting that trade imbalances reflect economic fundamentals, but are not inherently economically "bad" nor do they portend future bad economic news. Fundamentally, the current account deficits reflect the attractiveness of US assets. Furthermore, empirical evidence suggests that large current account deficits have little impact on interest rates or foreign exchange rates. Interest rates are a function of real economic growth, inflation expectations, and Fed policy. Foreign central banks have been purchasing US Treasuries and other US fixed income assets for policy reasons that are not necessary related to these three reasons that drive interest rates. Mr. Levy thinks that there are no current catalysts on the horizon to change foreign central bank policy.

The meeting adjourned at 4:15 p.m.

The Committee reconvened at the Hay-Adams Hotel at 5:35 p.m. The following members of the Committee were not present: Thomas Marsico and Richard Davis. The Chairman presented the Committee report to the Acting Under Secretary for Domestic Finance, Brian Roseboro and Deputy Assistant Secretary for Federal Finance, Tim Bitsberger. A brief discussion followed the Chairman's presentation but did not raise significant questions regarding the report's content.

The meeting adjourned at 6:00 p.m.

Jeff Huther
Director
Office of Debt Management
February 3, 2004

Certified by:
Mark B. Werner, Chairman
Treasury Borrowing Advisory Committee
of The Bond Market Association
February 3, 2004

Treasury Borrowing Advisory Committee Quarterly Meeting Committee Charge

Sensitivity of Financing Needs to GDP Estimates

We showed some of the financing risk associated with proposed or potential legislation at the last Committee meeting. We will now show the Committee slides on the uncertainty of our financing needs due to macroeconomic variables including real GDP, inflation and interest rates. Given this sensitivity and the central forecast of our borrowing needs, we would like the Committee's advice on whether Treasury's financing calendar provides sufficient flexibility.

Treasury Inflation-Protected Securities

We believe our current issuance calendar can meet the government's projected financing needs. We are also committed to further growing the TIPS market. We would like the Committee's advice on what criteria to use to assess our overall portfolio composition, keeping in mind our need to balance short and long term issuance as well as both nominal and TIPS issuance.

Changes to Auction Calendar

The November refunding calendar is complicated by several potential market-moving events and Veterans Day. We would like the Committee's advice on the scheduling of auctions in the final quarter of this year.

Financing this Quarter

We would like the Committee's advice on the following:

- The composition of Treasury notes to refund approximately $26.6 billion of privately held notes and bonds maturing on February 15.
- The composition of Treasury marketable financing for the remainder of the January – March quarter, including cash management bills.
- The composition of Treasury marketable financing for the April – June quarter.

Other Issues

Are there other issues relating to the current state of the Treasury market that the Committee would like to bring to Treasury's attention?

Related Documents:

- Q1 Tables
- Q2 Tables

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 4, 2004
JS-1139

**Report to the Secretary Of The Treasury
from the
Treasury Borrowing Advisory Committee
of the
Bond Market Association**

February 3, 2004

Dear Mr. Secretary:

Since the Committee's last meeting on November 4th, the economy has continued to grow at a robust pace. GDP expanded at a 4% pace in Q4 of 2003 following the 8% pace in Q3 of 2003. Moreover, the latest economic readings point to a continuation of strong growth in the first half of 2004. The ISM manufacturing report for January hit a 20-year high of 63.6. The latest 4-week average of mortgage applications for home purchases hit a record high, pointing to a continued strong housing market. The stronger trend in consumer spending since the fall is set to be further reinforced by unusually large tax refunds over the next few months as a result of the 2003 tax cuts. In contrast to this strength, growth in payrolls has remained slow, averaging 48,000 per month over the past three months. However, both continuing declines in initial claims and the result of business surveys suggest that an upturn in hiring is likely over the next few months. Consensus for this week's payroll report is expected to show that 160,000 new jobs were added in the month of January.

Commodity prices, including energy prices, have been rising rapidly. These increases have not yet translated into higher core inflation. To the contrary, the latest reading for the core PCE price index slowed to a new low for the cycle at 0.7%. The annual rate of inflation has fallen below 2% to 1.9%.

The Treasury market has been range-bound over the last three months and yields have fallen modestly since our last meeting: 2-year yields have fallen by approximately 10bp to 1.83% despite having risen to 2.10% during the period. The 2-year/10-year curve has flattened 12bp over the same period.

In line with a strong economic and corporate earnings performance, equity markets continue to improve as well: the S&P 500 Index has risen approximately 8%, and the NASDAQ composite has risen approximately 6% over the past three months. Furthermore, a pick up in M&A activity would indicate an improvement in corporate confidence.

Despite continued strong economic growth, the dollar has maintained its downward trend over the past quarter. It has weakened approximately 8% relative to the Euro and approximately 4% relative to the Japanese Yen.

Compared to previous quarters, budget expectations have been relatively stable. While there is some disparity in opinion among private forecasters about the longer-term budget outlook, most expect the budget deficit to be close to official expectations over the next two to three years.

Against this economic and financial backdrop, the members of the Committee began consideration of debt management questions included in the Quarterly Charge. Following their new format, Treasury presented a chart package that will be released as part of the Treasury refunding announcement.

The first section of the package considers the sensitivity of financing needs to economic factors. Treasury discussed at a previous session that they believe their financing is subject to different sensitivity factors—legislative, economic and technical. In their slides they illustrated the uncertainty of their financing needs due to economic variables including GDP, inflation and interest rates. The question asked of the Committee was "does the Treasury financing calendar provide sufficient flexibility?"

The first two charts outlined Treasury's financial requirements for the first and second quarters of 2004. These projections had already been released to the public.

The following charts considered the economic risk to the fiscal outlook. The charts demonstrate the volatility of expected outcomes to the market. One member of the Committee recommended that Treasury make the sensitivity analysis portion of the package standard in each quarterly release. By so doing, Treasury will be better able to communicate its borrowing needs under a variety of potential outcomes.

The Committee raised questions concerning the composition of Treasury's forecasting models. While Treasury was comfortable that their models capture a wide number of potential outcomes, the Committee encouraged them to continue to refine these explanatory variables—both short term and long term—and to share them with market participants.

The Committee largely agreed that the risk to the issuance calendar is minimal. During the past year, new 3-year notes, a shift to monthly 5-year notes and the reopening of 10-year notes have all been implemented by Treasury. The Committee felt this evidences a high degree of flexibility to the issuance calendar.

Treasury next asked the Committee's advice on what criteria to use in assessing the overall composition of its liability structure. Treasury re-emphasized its goals of increasing the amount of TIPS outstanding both nominally and as a percentage of total debt. Treasury also stressed its stated desire to balance short- and long-term debt issuance.

To that point, Treasury provided slides that showed projected issuance amounts of bills and notes well within bounds observed over the past twenty years. Treasury also provided a slide that showed projections of TIPS outstanding both as a percentage of issuance and as a percentage of total debt. Similarly, Treasury included slides focusing on the benefits and characteristics of TIPS suggesting that long-term investors tend to participate in the auction process and that state and local pension plans are investing more in the product. Lastly, Treasury stressed the diversification benefits of TIPS.

Committee members suggested several criteria by which to assess Treasury's choice of liability composition as they increase TIPS issuance. Some members felt that flexibility and liquidity concerns should predominate. Others felt that the level and direction of nominal rates in Treasury's decision-making process was also important. Members felt that Treasury would be well served to further study the variability of bill, note and TIPS issuance. Particularly, members felt that increasing the amount of TIPS outstanding could affect Treasury's cash flow in an appreciable manner without longer-term plans for bill and note issuance. Substitution of TIPS issuance for either note or bill issuance was viewed by most members as a viable strategy given the growing demand profile for the product.

Treasury then asked the Committee to offer its advice as to the scheduling of the November 2004 refunding and offered three potential options. The Committee agreed to consider the options and discuss this charge at the next meeting. The scheduling at the November refunding is complicated by the general election, a

meeting of the FOMC and a national holiday.

The Committee then addressed the question of the composition of Treasury notes to refund approximately $11.82 billion of privately held notes and bonds maturing on February 17th as well as the composition of Treasury marketable financing for the remainder of the January-March quarter, including cash management bills and for the April-June quarter. To refund $11.82 billion of privately held notes and bonds maturing February 17, 2004, the Committee recommended a $24 billion 3-year note due 2/15/07, a $16 billion 5-year note due 2/15/09, and a $17 billion 10-year note due 2/15/14. For the remainder of the quarter, the Committee recommended a $26 billion 2-year note issued in February and a $27 billion 2-year note issued in March, a $16 billion 5-year note issued in March, a $13 billion reopening of the 10-year note in March and a $8 billion reopening of the 10-year TIPS in April. The Committee also recommended a $20 billion 11-day cash management bill issued 3/4/04 and maturing 3/15/04. For the April-June quarter, the Committee recommended financing as contained in the attached table. Relevant features include three monthly 2-year notes (one of $27 billion, and two of $28 billion), three monthly 5-year notes (one of $16 billion and two of $18 billion), a $26 billion 3-year note, a $19 billion 10-year note issued in May followed by a $15 reopening of that 10-year note in June. The Committee further recommended a $12 billion 20-year TIPS for issuance in April.

Respectfully submitted,
Mark B. Werner
Chairman

Ian Banwell
Vice Chairman

Report(s):

- Q1 Tables
- Q2 Tables

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

January 29, 2004
JS-1142

Remarks of
Michael A. Dawson
Deputy Assistant Secretary
for
Critical Infrastructure Protection and Compliance Policy
at the Conference on
Protecting the Financial Sector and Cyber Security Risk Management
Organized by the
Federal Deposit Insurance Corporation
Philadelphia, Pennsylvania

"Protecting the Financial Sector from Terrorism and Other Threats"

I am pleased to be here in Philadelphia today. With over ten major insurance companies, a U.S. Mint, a Federal Reserve Bank, and one hundred FDIC-insured institutions, Philadelphia houses a significant portion of the critical financial infrastructure of the United States. In addition, the Philadelphia region is an important base for mutual fund companies, such as Vanguard, SEI Investments and Gartmore to name but a few. You, as owners and operators, are already working hard to protect your businesses, employees, and customers. Thank you for your efforts.

The purpose of this conference is to share with you some of the policies and programs that may further help your efforts at physical and cyber resilience and security. In partnership with the FDIC, the Department of the Treasury and our colleagues in the public and private sectors are holding conferences like this in twenty-four cities across the United States. During the conferences, we will reach thousands of professionals like you, owners and operators of our financial infrastructure. We hope you will take advantage of these policies and programs that can further strengthen the critical financial infrastructure of the United States.

Importance of Protecting Our Financial Infrastructure
The resiliency of the financial infrastructure is an issue that is very important to the Department of the Treasury. At the Treasury, we are responsible for developing and promoting policies that create jobs and improve the economy. We are also concerned with developing and promoting policies that enhance the resilience of the economy, policies that minimize the economic damage and speed economic recovery from a terrorist attack. Because of these responsibilities, the President named Treasury as the lead agency to enhance the resilience of the critical financial infrastructure.

These two responsibilities are closely related. As Secretary Snow has said, the financial system is the engine of our economy. In a very real sense, therefore, the resilience of the American economy depends on the resilience of the American financial system.

Fortunately, with an already resilient American economy, we are starting from a very strong base. Over the past few years, we have seen this resilience first hand, as the American economy withstood an economic recession, the terrorist attacks of September 11, corporate governance scandals, and the power outage of August 14-15. Many reasons have lead to the resilience of the American economy. Good policies like the President's Jobs and Growth Initiative played an important part.

So has the strength and resilience of the American people who are determined to protect our way of life.

Due in part to deregulation of the banking industry and innovation in technology, the American financial system is becoming increasingly more resilient. As recently as this Monday, Federal Reserve Board Chairman Alan Greenspan commented on this resilience, stating that "the more flexible an economy, the greater its ability to self-correct in response to inevitable, often unanticipated, disturbances and thus to contain the size and consequences of cyclical imbalances."

The successful performance of the financial system during the power outage of last August exemplifies this resilience. With one exception, the bond and major equities and futures markets were open the next day at their regular trading hours. Major market participants were also well prepared, having invested in contingency plans, procedures, and equipment such as backup power generators. The U.S. financial sector withstood this historic power outage without any reported loss or corruption of any customer data. This resilience mitigates the economic risks of terrorist attacks and other disruptions, both to the financial system itself and to the American economy as a whole.

Although we are starting from a strong base, the fact remains that terrorists continue to target the U.S. economy and U.S. financial institutions. Therefore, we must continue our vigilant efforts to protect our critical financial infrastructure.

Guiding Principles

Four principles guide our efforts to enhance the resilience of our financial infrastructure. These principles guided our actions as the financial system recovered from the attacks of September 11th. They guided our actions during the power outage of August 14-15. They guide our day to day actions as we prepare for the next disruption.

The first principle is to remember that the financial system is really about people. People, not buildings or computers, produce financial services. And it is people who benefit from financial services.

We depend on people - tellers, technicians, loan officers, technologists - to run the financial system and to see the system through during times of stress. Indeed, it was the commitment of these professionals to their institutions, customers, and colleagues that helped the financial system recover from the attacks of September 11th and weather the power outage of August 14-15.

Just as we depend on people to operate the financial system, people depend on the financial system to remain in operation. Every American depends on financial services to get their paycheck, buy their groceries, purchase a house, finance their children's education, or save for retirement. We must ensure that people continue to have confidence that the financial system will meet their needs.

The second principle is the importance of maintaining confidence. Confidence in the ability of financial institutions to clear checks, execute transactions, and satisfy insurance obligations helps the system weather significant disruption from evolving threats. By relying on a sound financial system, Americans can make business decisions for the future and conduct necessary business in the present.

The third principle is to ensure that the financial system remains accessible and open for business when the safety of the employees permits. During times of disaster, investors depend on markets to price the impact of the disruption on assets. The longer markets are closed, the longer investors must go without knowing what the impact will be. This uncertainty can itself be harmful to the economy, compounding the impact of any disruption. The sooner we can eliminate this uncertainty, the more we can mitigate the impact and speed recovery.

Fourth, we want to promote responsible decision-making and problem-solving within the private sector. In general, financial institutions should make the

appropriate decisions without waiting for guidance from Washington. After all, it is the private sector that owns and operates the majority of the financial systems, and therefore knows best how to mend these systems after a disruption.

Organization
With these principles in mind, we have organized ourselves into two main groups. One is the Financial and Banking Information Infrastructure Committee (FBIIC). The FBIIC is sponsored by the President's Working Group on Financial Markets and consists of many state and federal regulators. The FDIC, which organized this conference today, is a member. So too are the Board of Governors of the Federal Reserve System, the Securities and Exchange Commission, the Commodity Futures Trading Commission, the National Association of Insurance Commissioners, the Conference of State Banking Supervisors, and many other important regulators. Treasury chairs the FBIIC.

The other important group is the Financial Services Sector Coordinating Council (FSSCC). The FSSCC consists of virtually every important financial services association in the United States.

The structure of these organizations advances the principles I just spoke about. As the President stated in his National Strategy for the Physical Protection of Critical Infrastructures and Key Assets, "it is important to remember that protection of our critical infrastructures and key assets is a shared responsibility. Accordingly, the success of our protective efforts will require close cooperation between government and the private sector at all levels." These two organizations facilitate that close cooperation and encourage private sector responsibility to protect the critical financial infrastructure without adding unnecessary layers of bureaucracy.

Policies
The four principles - protecting people, maintaining confidence, maintaining access to financial institutions, and promoting de-centralized decision-making and responsibility - shape our policies to enhance the resilience of the U.S. economy. For example, they highlight the importance of developing accurate and timely information about threats and sharing that information with the private sector. As we share more and better information about threats, people in the private sector who own and operate our financial infrastructure can better estimate the risks they bear and can more effectively reduce the probability of a disruption through strategic investments.

Furthermore, as more institutions invest in better security measures, the incentive for other firms to invest will also increase as they realize they might be left behind the competition. This tipping or cascading effect on businesses provides a very efficient and effective means of encouraging optimal investment in our corporate resilience. It also reduces the need for the government to impose costly, inflexible, and potentially ineffective command-and-control security regulations on the private sector.

Programs
I wish to highlight a few of the programs that we have developed. These programs provide you with specific, tangible services that can help make your institutions and your colleagues safer.

Recently, the FBIIC and the FSSCC launched the next generation Financial Services Information Sharing and Analysis Center (FS/ISAC). Since 1999, the FS/ISAC has been a leader in information sharing for the financial sector, allowing members to receive and submit anonymous reports on security threats and solutions. This next generation FS/ISAC, which now serves the entire financial sector, includes both cyber and physical threat information and deploys a secure, confidential technology platform where companies can exchange information in real time as they identify vulnerabilities, address the vulnerabilities, and respond to attempts to exploit the vulnerabilities.

Given the benefits of increased information sharing with the general public, Treasury is pleased to support the next-generation FS/ISAC. I hope that all of you

will consider joining the FS/ISAC as members. You can learn more about how your financial institution can benefit from the FS/ISAC at www.fsisac.com.

Another important program is the Government Emergency Telecommunications Service (GETS) program. This program, which is run by the National Communications Service, provides critical members of the private sector priority access to the telecommunication system. In times of emergency when the telephone system experiences heavy traffic, GETS users can complete their calls faster so that they may discuss and coordinate emergency decisions. Since the attacks of September 11, the GETS program has expanded more than six-fold within the financial sector. If you are interested in participating in this program, please contact your primary regulator. Each of the participating regulators serves as the administrative sponsor for the GETS program. If you are already a GETS user, please remember to test your cards on a quarterly basis.

A third important program that the Treasury created is the Protective Response Planning Program. This program brings together federal and local government officials, members of law enforcement and individuals from important financial institutions to develop and coordinate emergency responses to major disruptions at these specific institutions.

During these exercises, government officials - from the local police chief, to the county sheriff, the state police superintendent, the FBI, the United States Secret Service, and still others coordinate their emergency response plans, in some cases for the first time. The success of these exercises have demonstrated the power of a truly collaborative effort. The Protective Response Planning Program is open to the most critical financial institutions. If you are interested, please contact me.

Thank you for your time today. Thank you for attending this important conference.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 3, 2004
JS-1143

**Statement on the President's Fiscal Year 2005 Budget
by
Treasury Secretary John Snow
before the
Committee on Ways and Means
Tuesday, February 03, 2004**

Thank you, Mr. Chairman.

Thank you all for having me here today to talk about the President's budget.

I believe you'll find that this budget reflects the priorities of our nation as well as the leadership of President George W. Bush.

The over-riding theme of the budget, and the President's plan for the future, is that a safer world is a more prosperous world. That's why I'll be discussing both national and economic security here today.

Overview of the President's Priorities

Decisions about how to collect and spend taxpayer dollars – for this is what a budget is – must be made with both caution and vision.

The Fiscal Year 2005 budget proposal is, therefore, a plan that does three core things:

One: Keeps Americans safe by providing the resources necessary to win the war on terror and protect our homeland;
Two: Increases the economic security of our citizens as well, by strengthening our economy; and
Three: Exercises the kind of spending discipline that is required by a government that respects the source of its money (hard-working taxpayers!) and is unwilling to live with a deficit.

Discussions of our budget and our economy are not, and should not, be separate. The two are inextricably connected.

Today, our economy is doing better.

Homeownership is up, unemployment rates are heading down, and GDP growth has been extremely strong.

This administration came to office when those indicators were not nearly as positive.

The President inherited an economy that was in decline... one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

The President and his administration took these challenges seriously and we have made serious progress in changing the economic direction of this country.

The President's tax cuts – passed by you – have worked. They provided the

stimulus that was necessary to turn the economic ship around... and they are now encouraging and allowing for the economic growth that is continuing into the future.

Economic growth in the second half of 2003 was the fastest since 1984;
New home construction was the highest in almost 20 years;
Homeownership levels are at historic highs;
Manufacturing activity is increasing;
Inflation and interest rates are low;
Over a quarter million jobs were created in the last five months of 2003.
Unemployment claims – both initial claims and continuing claims – are falling, indicating improvement in the labor market;
And last Monday, the Dow closed at a 31-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: We are on a path to sustained economic growth.

However, there is more to do. We are not, by any means, satisfied.

There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

Our budget addresses that need by continuing to focus on improving our economy.

For example, the President's Jobs for the 21st Century plan, announced in his State of the Union Address, directs the resources of several branches of government toward matching skills with jobs, and helping workers acquire the skills they need to qualify for the jobs in their community.

We can also encourage the creation of jobs by sticking to the President's six-point plan for growth.

That includes making health care more affordable and costs more predictable.

We can do this by passing Association Health Plan legislation that would allow small businesses to pool together to purchase health coverage for workers at lower rates.

We also need to promote and expand the advantages of using health savings accounts ... how they can give workers more control over their health insurance and costs.

And we've got to reduce frivolous and excessive lawsuits against doctors and hospitals. Baseless lawsuits, driven by lottery-minded attorneys, drive up health insurance costs for workers and businesses.

The need to reduce the lawsuit burden on our economy stretches beyond the area of health care. That's why President Bush has proposed, and the House has approved, measures that would allow more class action and mass tort lawsuits to be moved into Federal court -- so that trial lawyers will have a harder time shopping for a favorable court.

These steps are the second key part of the President's pro-jobs, pro-growth plan.

Ensuring an affordable, reliable energy supply is a third part.

We must enact comprehensive national energy legislation to upgrade the Nation's electrical grid, promote energy efficiency, increase domestic energy production, and provide enhanced conservation efforts, all while protecting the environment.

Again, we need Congressional action: we ask that you pass legislation based on the President's energy plan.

Streamlining regulations and reporting requirements are another critical reform

element that benefit small businesses, who represent the majority of new job creation: three out of every four net new jobs come from the small-business sector! Let's give them a break wherever we can so they're free to do what they do best: create those jobs.

Opening new markets for American products is another necessary step toward job creation. That's why President Bush recently signed into law new free trade agreements with Chile and Singapore that will enable U.S. companies to compete on a level playing field in these markets for the first time -- and he will continue to work to open new markets for American products and services.

Finally, we've got to enable families and businesses to plan for the future with confidence.

That means making the President's tax relief permanent.

Rate reductions, the increase in the child tax credit and the new incentives for small-business investment – these will all expire in a few years. The accelerated rate reductions that took effect in 2003 will expire at the end of this year. Expiration dates are not acceptable – we want permanent relief.

The ability of American families and businesses to make financial decisions with confidence determines the future of our economy. And without permanent relief, incentives upon which they can count, we risk losing the momentum of the recovery and growth that we have experienced in recent months.
The tax relief is the key stimulus for increased capital formation, entrepreneurship and investment that cause true economic growth.

Budgets work better when the economy is growing... because a growing economy means more jobs. That means more tax revenue... which leads to all-important deficit reduction.

Which leads me to my next area of discussion.

Overview of the Budget Deficit Situation

Let me be clear on this:
The budget deficit that we face today is unwelcome.
It needs to be addressed.
The President's budget calls for cutting the deficit in half over the next five years.
Wile addressing the deficit, we must remember that it is not historically overwhelming.
It is understandable, given the extraordinary circumstances of recent history.
Remember that we are fighting a type of war that we have never fought before. We are fighting an enemy that requires a much broader variety of government resources than anything we've ever confronted. And we began this fight when we were economically wounded.

What's most important to remember is that we will be able to fight this war and climb out of the deficit.

We can manage this deficit, and we can cut it in half over the next five years by controlling spending and growing our economy.

Three-quarters of the discretionary spending increases during this Administration have been related to the global war on terror and the response to 9/11.

Meanwhile, President Bush has reduced the rate of increase in non-security-related spending every year he has been in office: to six percent in 2002, five percent in 2003, and to four percent in the current fiscal year.

For Fiscal Year 2005 we're going to reduce the rate of increase in non-security spending to less than one percent.

Total annual appropriated spending will increase by less than four percent next year.

Holding the line on spending – while ensuring that our country is safe and our most important needs, from jobs to health care, are met – will achieve deficit reduction when coupled with all-important economic growth.

Again, this is why the budget cannot be discussed separately from the economy. Separating the two is what gets government into trouble.

Make no mistake; President Bush is serious about the deficit.

We see it as unwelcome, but manageable... and we intend to achieve: rapid deficit reduction.

A recent CBO report raised concerns about this matter, and it is important to note that recent and short-term projected budget deficits and the existence of long-term deficits for Social Security and Medicare are not connected.

These unfunded long-term net obligations are also a concern, and ones that this Administration has highlighted and invited bipartisan dialogue on.

The President has been clear on this: younger workers should have the opportunity to build a nest egg by saving part of their Social Security taxes in personal retirement accounts. His vision for the program is economically wise, and it is that we should make the Social Security system a source of ownership for the American people.

Conclusion

Are we dedicating ourselves to increased spending on the war on terror and protecting the homeland? The answer is yes. Yes, without sacrificing other necessities.

And that is because a nation must be safe in order for it to be prosperous.

A nation of entrepreneurs must also be able to plan, and to be relieved of as many burdens as possible, in order to be prosperous.

All of the budget issues and policy proposals that I've discussed today may seem, at times, to be a complicated recipe. But these ingredients combine to make something that is simply put, and is of utmost importance – and that is economic growth.

Growth is the key to every economic problem we confront. That's why we urge other countries to institute pro-growth policies. It's good for them, and it's good for the global economy that we are a significant part of.

Thank you for hearing my testimony today. I'll be happy to take your questions now.

PRESS ROOM

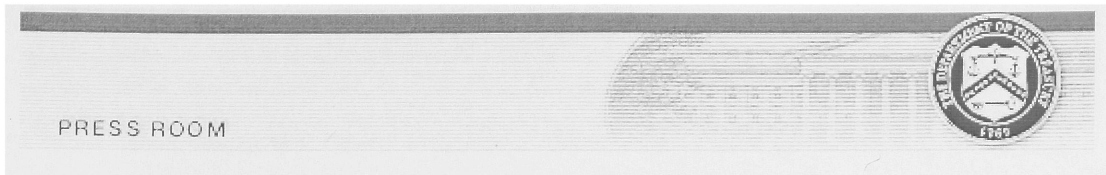
FROM THE OFFICE OF PUBLIC AFFAIRS

February 3, 2004
JS-1144

Statement of Under Secretary John B. Taylor Regarding the Decisions by Countries to Issue Bonds with Collective Action Clauses (CACs)

Statement of Under Secretary John B. Taylor Regarding the Decisions by Countries to Issue Bonds with Collective Action Clauses (CACs)

The United States strongly supports and welcomes the decision of a growing number of countries to include collective action clauses in external bond issues. Since the New Year, Chile, Panama, Colombia, Costa Rica and Venezuela completed successful bond issues, including CACs for the first time, while Brazil, Turkey and Mexico's recent issues again included CACs. Belize, Guatemala, Korea, Italy, Peru, Poland, South Africa and Uruguay included CACs in bond issues last year. These nations are helping make collective action clauses the market standard in external sovereign bond issues under New York law, and strengthening the international financial system. The Treasury encourages all countries that issue external bonds under New York law to include collective action clauses in their offerings.



FROM THE OFFICE OF PUBLIC AFFAIRS

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February 2, 2004
js-1145

Treasury Releases "2004 Blue Book"

On February 2, 2004 the Treasury Department released the General Explanations of the Administration's Fiscal Year 2005 Revenue Proposals, the document also known as the "Blue Book."

The text of the 2004 Blue Book is attached.

Related Documents:

- Blue Book

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 4, 2004
JS-1146

Statement on the President's Fiscal Year 2005 Budget
by
Treasury Secretary John Snow
before the
House Committee on the Budget
Wednesday, February 04, 2004

Thank you, Mr. Chairman.

Thank you all for having me here today to talk about the President's budget.

I believe you'll find that this budget reflects the priorities of our nation as well as the leadership of President George W. Bush.

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Growth is the key to every economic problem we confront. That's why we urge other countries to institute pro-growth policies. It's good for them, and it's good for the global economy that we are a significant part of.

Thank you for hearing my testimony today. I'll be happy to take your questions now.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 4, 2004
JS-1147

Remarks of Wayne A. Abernathy
Assistant Secretary of the Treasury for Financial Institutions
American Enterprise Institute
Washington, D.C.
Formula One Regulation for GSEs

It is a pleasure to be here at AEI today, to leave the Do Tank to spend some time at a Think Tank. I am not embarrassed to reveal, having spent virtually my whole career at one place or another in government, that people in government draw a lot of water from the deep wells of thought and creativity found in places such as the American Enterprise Institute. I make little claim to original thinking, but I do make a claim to being able to recognize good thinking. And I am not shy to make use of someone else's good ideas. I consider it part of the package enshrined in the constitutional right to petition government.

I like to say, because it is true, that I get my best ideas by listening to the people who have to live with the consequences of decisions made here in Washington. So I take every opportunity to talk with business people and with their customers, when they come to Washington, and when I travel throughout the country.

Let me cite an excellent example. We recently passed an important piece of legislation, the Fair and Accurate Credit Transactions Act of 2003. Early last year, President Bush determined that we need to give consumers, law enforcers, and businesses new tools to fight identity theft.

But what tools would work? We found out by consulting with victims of identity theft, with law enforcement people, with regulators, with businesses. The result was a powerful, important piece of legislation that President Bush signed into law in December, that will strengthen the ability of consumers, law enforcement people, and businesses to deter identity theft, to increase the chance of catching the thieves, and to reduce the time it takes for victims to restore their good name.

A lot of thought went into that bill. Not all of the thoughts we heard went into the bill. Some ideas we heard were impractical, some not appropriate for the federal level, some would have been counterproductive. But we heard a lot of good thoughts, came up with a couple of our own—inspired by ideas that people shared with us—and they made up the bill. This year we are in the process of implementing that legislation. For a long time, many identity thieves have had it easy. They won't have it so easy anymore.

I want to congratulate AEI for doing a lot of thinking, and encouraging others to do a lot of thinking, for a long time, about our system of government sponsored enterprises, particularly the GSEs that are chartered to focus on housing: Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. We appreciate the high priority that you have placed upon them, because this Administration places a high priority on them as well.

It is no secret that these housing GSEs have an inadequate system of supervision. And it is a poorly kept secret, that they have never had an adequate system of supervision.

I am quick to admit that the supervision of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks has in fact improved recently. Supervisory resources are greater and better focused, the regulators are hard-nosed about doing their job. But despite the best efforts of the current leadership of the GSE supervisors, there is only so much that they can do. There is only so much that can be done with the

limited authorities and resources and stature that have been granted to these regulators under the existing law. The GSE supervisors today are working hard with what they have. They show no signs of letting up or easing off, and yet it is not enough. The law does not give them what they need to do their job.

We have the world class—the world-leading—housing finance system, but we do not have a world class supervisory system.

What do we do about it? That is the theme of the series of conferences that you have held. And your conferences, and others on this subject, are stirring up people's minds, getting the thought processes moving. They are stimulating fundamental thinking. They are asking questions that need to be asked.

It is no surprise to many of you here, that while we strongly share and appreciate the sense of importance and timeliness of the focus, the Administration does not support the calls for "privatizing" the housing GSEs.

Fannie Mae and Freddie Mac have special status in the housing finance market because they were created by Congress for a specific purpose: to increase homeownership among low- and moderate- income families by creating a strong secondary market to make it easier for these families to secure loans to buy homes. The Administration shares that original commitment, and wants to ensure that GSEs live up to their responsibilities, in a way that strengthens the safety and soundness of mortgage markets and the economy at large. And that is part of the reason why we believe that meaningful substantive reform is needed.

Moreover, the accounting issues and management issues and earnings issues that arose over the last year with respect to Fannie, Freddie, and several of the Home Loan Banks give us good reason to avoid being complacent.

There is a metaphor that appeals to me. Congress created Fannie, Freddie, and the Home Loan Banks as muscular workhorses to help with the plowing—and it was tough, hard plowing at first. Congress put them in harness, to serve important national purposes of promoting homeownership. Our focus at the Administration is on how best to control the reins to ensure that these housing workhorses focus their strength on straight and deep furrows, rather than on how to cut the reins and see what they might do if left free to wander the pasture.

That control takes strong, effective hands. For that reason, while the Administration does not support proposals for privatization of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks, we also cannot support continuation of the status quo. In fact, no one interested in promoting home ownership in this nation should be satisfied with the status quo. We need a stable, dependable system of housing finance to achieve and sustain the highest levels of homeownership, now and in the future.

We are making great progress. In 2002, President Bush announced the goal of this Administration to increase the number of minority homeowners by 5.5 million before the end of the decade. We are ahead of schedule. Already more than one and a half million minority families have moved into their own home since the announcement of the President's goal. Statistics announced just yesterday reveal that for the first time ever, more than half of minority households own the home they live in, and our national homeownership rate set a new record.

But there is still a lot more work to do, and we are doing it. On December 16, 2003, the President signed into law the American Dream Downpayment Act of 2003, to help approximately 40,000 families a year with their down payment and closing costs, and further strengthen America's housing market.

That is why we are so determined to bring a new, higher standard of supervision and accountability for Fannie, Freddie, and the Federal Home Loan Banks, because we are going to expect them to do even more to expand homeownership. Second best will not do. We need a supervisor that has all of the authority—including the stature and power to wield that authority consistently—that we would look for in any credible financial regulator. That includes the authority to review the new activities of these government-sponsored enterprises. Since the government sponsored them, then the government should be able to examine what they propose to do with that sponsorship.

What we do support is a prudential supervisor for Fannie, Freddie, and the Federal Home Loan Banks that has full authority to set prudent capital levels, both minimum and risk-based capital.
Some would suggest that authority over risk-based capital is all that is needed, that if you are setting capital standards based entirely on risk, what more is wanted?

Just last week I had a frank conversation with some market place experts, experts in GSE securities. I asked them, has the art of regulatory risk-based capital progressed to the point where it captures all of the risk, where we do not need minimum capital standards? They shook their heads, and said, "No." I have not yet found capital market experts who would argue otherwise, or, more importantly, who would invest significant money on any other basis than a foundation of strong, minimum capital.

There remain risks that we cannot yet quantify, that we cannot yet fully predict, that we cannot yet fully account for. Until we can, for the unknown, unknowable, or simply unpredictable and unidentifiable risks, we will need minimum capital. And the regulator needs full authority to define what that minimum capital level is, and to change it as circumstances warrant.

I will tell you what else we support. We support a regulator with full receivership authority for the orderly resolution of a government sponsored enterprise that gets into serious financial difficulty. That includes full authority for the fair and equitable distribution of assets to avoid a legal free-for-all that could disrupt and disorganize our housing finance markets. That means all the authority to wind up affairs in an orderly manner—reserving for Congress, in the case of Fannie and Freddie, the power to revoke charters.

We support an independent funding source, outside of the appropriations process, as Congress has already created for the federal bank, thrift, and credit union supervisors. When Congress was recently forced into a Continuing Resolution to fund the government over the holidays, a lot of important programs were put on hold. One of those was the much needed increase in resources for Fannie Mae's regulator to hire the extra manpower to review the condition of Fannie Mae's books. That crucial regulatory need was put on hold while Fannie Mae's regulator waited for budget authority, authority that would be paid for entirely by Fannie Mae and Freddie Mac, but which law requires the Congress to sign off on first. We should not make the regulator of two of the four largest financial institutions in the country wait each year for an Act of Congress to get the resources to do its job.

And we can support placing this new regulator within the Treasury Department, provided some basic standards are met to ensure that doing so will strengthen the supervisory structure we are creating, and not interfere with another important job at Treasury, the wise and efficient receipt and use of taxpayer resources. A case involving the Comptroller of the Currency demonstrates why that is so important. Last year the supervisor of national banks, the Comptroller of the Currency, prohibited certain national banks from renting their charter to so-called payday lenders. Under this practice, a payday lender would pay a national bank to set up operations in the bank's name, but the bank would have little say over the payday lender's operations. Under such a scheme, the bank took on some financial risk, but it took on enormous reputational risk.
So the Comptroller said, "You can't do that. The reputation of the national bank charter is too important."

We cannot allow, no one in this nation should be willing to tolerate, renting the Treasury's charter, its good name. But that is what we would be doing if we placed a new regulator under the shield of the Treasury, but blocked the Treasury Secretary from any meaningful role in the key policies of that agency.

A reporter not long ago asked me, where is the compromise in the Administration's position? I replied that the question misunderstood the approach taken by the Administration to the problem of adequate financial supervision. We did not begin this process by trying to stake out an excessive position from which to begin bidding. We conducted a detailed and thorough study to identify what are the minimum elements of credible financial supervision. We asked, what are the fundamentals?

The result was the identification of a few key, first principles of prudential supervision that make for a safe and sound supervisory system. There cannot be

and should not be any credibility in a system that is less than safe.

Earlier, I used the analogy of a work horse, which I think very appropriately applies to the important, fundamental mission assigned to our housing GSEs. Let me now call upon another analogy that helps to understand the complex and sophisticated financial institutions they have become.

I point you to the world of Formula One racing. From the perspective of speed and technology, Formula One racing is at the top of the racing art. This from the official website of Formula One racing:

"A modern Formula One car has almost as much in common with a jet fighter as it does with an ordinary road car."

These cars achieve top speeds in excess of 200 mph. At these speeds the tolerance for error is small. A small error may mean more than the loss of a race; it may spell disaster for the driver and serious harm to other participants.

A lot of people have a lot of fun with the statistics that apply to our GSEs, probably because it is so hard to grasp mentally the size of these institutions. Here are a few statistical forays: Fannie Mae, Freddie Mac, and the Federal Home Loan Banks include two of the four largest financial institutions in the United States. Only about 10 banks or thrifts in the United States have more assets than the largest Federal Home Loan Bank, and fewer than 40 have more assets than the smallest. Collectively, they offer more securities to the financial markets each year than does the U. S. Treasury. Fannie and Freddie have about 40 per cent of the secondary mortgage market, and so on.

The point is, they are big, very big. And their importance for our financial markets in general and our housing markets in particular is big. In this case, size matters. They are in the top tiers of financial institutions. At this size, the tolerance for error is small.

Again from the official Formula One website:

"The construction of Formula One cars and the materials used are strictly controlled by the regulations to maximise their safety.

"The main structure of the car comprises a safety cell which contains the cockpit plus the fuel tank, which is housed immediately behind (but separated from) the driver.

"This safety cell must meet minimum size requirements and must have an impact-absorbing structure immediately in front of it. The design of the car must also include an additional impact-absorbing structure at the rear, behind the gearbox."

As with Formula One racing, wonderful innovations and achievements can be encouraged and realized, because of important safety rules that are imposed and enforced. As the Formula One car has a safety cell to protect the driver, so must the GSE have capital requirements and other prudential standards tailored to protect the fundamental job of the GSE.

It is the view of the Administration that this kind of safety regime can be and must be created. In doing so, we provide for the safety of the spectators and the participants alike.

Keeping Fannie Mae, Freddie Mac, and the Federal Home Loan Banks on track means the highest safe speeds for our housing industry and all who benefit from it.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 4, 2004
JS-1148

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on Factory Orders and Non-Manufacturing Business Activity

Reports out today suggest economic activity continues to gain momentum. An index of non-manufacturing business activity jumped in January to its highest level on record. On the manufacturing front, factory orders rose in December to reach the highest level in three years suggesting we'll see further pickup in production. An index of manufacturing activity released earlier this week is at a twenty-year high.

These are encouraging signs which indicate the economy's fundamentals are strong. But there is more to be done, and this Administration will continue its efforts to strengthen the economy and boost job creation until every American looking for work can find a job.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 5, 2004
JS-1149

Statement by Treasury Spokesman Rob Nichols

After the G7 Meeting of Finance Ministers and Central Bank Governors in Boca Raton, Treasury Secretary John Snow will visit Miami, Tampa and Jacksonville, Florida February 9-10 to discuss U.S. policy towards Cuba and the President's plan to further strengthen the U.S. economy and create jobs.

On February 9th, in Miami, the Secretary will deliver remarks before an audience of Cuban Americans about the economic embargo against Castro's regime and our hopes for freedom for the Cuban people.

On February 10th, in Tampa, the Secretary will meet with local business leaders and then tour Sun State International Trucks, a full service truck dealership. Later that day in Jacksonville, the Secretary will tour Florida Community College's new Advanced Technology Center, which provides workforce training in the following emerging-economy career fields: information technology, biotechnology, advanced manufacturing and transportation technology.

More than 5 million taxpayers in Florida have lower income tax bills as a result of the President's recently enacted growth package.

A schedule of the Secretary's open press events will be posted on www.treasury.gov on Friday, February 6th.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 5, 2004
JS-1150

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on 2003 Fourth Quarter Productivity Report

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on 2003 Fourth Quarter Productivity Report

Building on the third quarter's strong productivity gains, we saw further growth in the fourth quarter of 2003. In the 12 quarters since the end of 2000, productivity has grown at a 4.1 percent annual rate, the most rapid three-year change in decades. Rapid productivity growth is making it more affordable to hire workers, boosting profit margins, and keeping inflation low.

In addition to recent good news including gains in manufacturing, growth in the services sector, higher consumer confidence and ongoing strength in the housing market, today's productivity report illustrates that a solid economic recovery continues. Yet, there is more to be done and we remain dedicated to ensuring that job opportunities are there for every American looking for work.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 5, 2004
2004-2-5-15-22-2-12208

U.S. International Reserve Position

The Treasury Department today released U.S. reserve assets data for the latest week. As indicated in this table, U.S. reserve assets totaled $85,368 million as of the end of that week, compared to $86,610 million as of the end of the prior week.

I. Official U.S. Reserve Assets *(in US millions)*

	January 23, 2003			January 30, 2004		
TOTAL		86,610			85,368	
1. Foreign Currency Reserves [1]	Euro	Yen	TOTAL	Euro	Yen	TOTAL
a. Securities	8,508	14,810	23,318	8,386	14,862	23,248
Of which, issuer headquartered in the U.S.			0			0
b. Total deposits with:						
b.i. Other central banks and BIS	13,774	2,975	16,749	13,606	2,986	16,592
b.ii. Banks headquartered in the U.S.			0			0
b.ii. Of which, banks located abroad			0			0
b.iii. Banks headquartered outside the U.S.			0			0
b.iii. Of which, banks located in the U.S.			0			0
. IMF Reserve Position [2]			22,744			22,887
. Special Drawing Rights (SDRs) [2]			12,755			12,598
Gold Stock [3]			11,043			11,043
Other Reserve Assets			0			0

II. Predetermined Short-Term Drains on Foreign Currency Assets

	January 23, 2003			January 30, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
'oreign currency loans and securities			0			0

.ggregate short and long positions in forwards and futures in foreign currencies vis-à-vis the U.S. dollar:

2.a. Short positions			0			0
2.b. Long positions			0			0
3. Other			0			0

III. Contingent Short-Term Net Drains on Foreign Currency Assets

	January 23, 2003			January 30, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
1. Contingent liabilities in foreign currency			0			0
1.a. Collateral guarantees on debt due within 1 year						
1.b. Other contingent liabilities						
2. Foreign currency securities with embedded options			0			0
3. Undrawn, unconditional credit lines			0			0
3.a. With other central banks						
3.b. With banks and other financial institutions						
Headquartered in the U.S.						
3.c. With banks and other financial institutions						
Headquartered outside the U.S.						
4. Aggregate short and long positions of options in foreign						
currencies vis-à-vis the U.S. dollar			0			0
.a. Short positions						
.a.1. Bought puts						
a.2. Written calls						
b. Long positions						
b.1. Bought calls						
).2. Written puts						

Notes:

cludes holdings of the Treasury's Exchange Stabilization Fund (ESF) and the Federal Reserve's System Open Market Account MA), valued at current market exchange rates. Foreign currency holdings listed as securities reflect marked-to-market values, and)sits reflect carrying values. Foreign Currency Reserves for the latest week may be subject to revision. Foreign Currency

Reserves for the prior week are final.

2/ The items, "2. IMF Reserve Position" and "3. Special Drawing Rights (SDRs)," are based on data provided by the IMF and are valued in dollar terms at the official SDR/dollar exchange rate for the reporting date. The entries for the latest week reflect any necessary adjustments, including revaluation, by the U.S. Treasury to IMF data for the prior month end.

3/ Gold stock is valued monthly at $42.2222 per fine troy ounce.

ıblic Debt Announces Activity for Securities in the STRIPS Program for nuary 2004

R IMMEDIATE RELEASE

ruary 5, 2004

Bureau of the Public Debt announced activity for the month of January 2004, of securities within the Separate Trading of Registered ·est and Principal of Securities program (STRIPS).

	In Thousands
cipal Outstanding (Eligible Securities)	$2,578,568,532
l in Unstripped Form	$2,402,044,105
in Stripped Form	$176,524,427
ınstituted in December	$12,462,630

ccompanying table, gives a breakdown of STRIPS activity by individual loan description. The balances in this table are subject to and subsequent revision. These monthly figures are included in Table V of the Monthly Statement of the Public Debt, entitled ngs of Treasury Securities in Stripped Form."

TRIPS table, along with the new Monthly Statement of the Public Debt, is available on Public Debt's Internet site at: ꞁublicdebt.treas.gov. A wide range of information about the public debt and Treasury securities is also available at the site.

- 1151

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 6, 2004
JS-1152

Statement of Secretary John Snow on January Employment Report

Today's report on employment marks the fifth straight month of job growth, pushing the number of jobs created over the past five months to over 360,000. The unemployment rate has continued to drop since its peak in June, the largest seven-month decline since 1995. We're seeing solid gains in the underlying fundamentals. Manufacturing is showing signs of progress, a services sector index hit its highest level on record in January, consumer confidence is improved, and the housing market continues to be a base of strength for the economy. Following exceptional GDP growth in the third quarter, 2003 ended on solid ground, coming in above the historical average. The President's Jobs and Growth Act, which provided needed tax relief for millions of American families, continues to boost economic activity and improve the environment for job creation.

I'm pleased by the strength of the recovery underway, but not satisfied. The President will persist in his efforts to drive economic growth and job creation until every American looking for work can find a job.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 6, 2004
JS-1153

Treasury Issues Guidance to Clarify Treatment of Environmental Remediation Costs

Today the Treasury Department and the IRS issued two revenue rulings to clarify the tax treatment of hazardous waste clean-up costs.

The first, Revenue Ruling 2004-17, clarifies that the money taxpayers spend in a current taxable year to clean up environmental contamination that occurred in previous years does not qualify for a special rate adjustment.

The second, Revenue Ruling 2004-18, clarifies that the money taxpayers spend for hazardous waste clean up costs may have to be capitalized into inventory costs.

Related Documents:

- Revenue Ruling 2004-17
- Revenue Ruling 2004-18

Part I

Section 1341.BComputation of Tax Where Taxpayer Restores Substantial Amount Held Under Claim of Right

26 CFR 1.1341-1: Restoration of amounts received or accrued under claim of right. (Also ' 263A.)

Rev. Rul. 2004-17

ISSUES

Do amounts paid or incurred in the current taxable year to remediate environmental contamination that occurred in prior taxable years qualify for treatment under ' 1341 of the Internal Revenue Code?

FACTS

Situation 1

N manufactures products that it sells to wholesalers and retailers. *N*=s manufacturing process creates hazardous waste. *N* uses an accrual method of accounting and the calendar taxable year. From the inception of its business in 1950 until 1979, *N* buried the hazardous waste on land that it owned in accordance with then applicable state, federal, and local environmental laws. *N* accounted for waste disposal costs as a deducible expense under § 162.

Significantly stricter state, federal, and local hazardous waste disposal laws were enacted in later years. In 2004, in order to comply with current environmental laws, *N* incurs expenses for all necessary services to eliminate soil and water contamination caused by the buried waste, transport the waste to a waste disposal facility that complies with current environmental laws, and restore the land.

Situation 2

The facts are the same as in *Situation 1* except that *N* accounted for waste disposal costs as a production cost in calculating its inventory costs for all years.

LAW AND ANALYSIS

Section 1341 applies if: (1) the taxpayer included an item in gross income for a

prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to the item, (2) a deduction is allowable to the taxpayer for the taxable year because it was established after the close of the taxable year (or years) of inclusion that the taxpayer did not have an unrestricted right to the item or to a portion of the item, and (3) the amount of the deduction exceeds $3,000. Section 1341(a)(1) - (3).

If ' 1341 applies, the chapter 1 tax for the taxable year equals the lesser of: (1) the tax for the taxable year computed with the current deduction, or (2) the tax for the taxable year computed without the deduction, less the decrease in tax for the prior taxable year (or years) that would have occurred if the item or portion thereof had been excluded from gross income in the prior taxable year (or years). Section 1341(a)(4) and (5). Section 1341 ensures that the taxpayer=s position is not worse than the position the taxpayer would have been in if the taxpayer had not included the item or portion thereof in gross income in the earlier year (except for the time value of money).

Section 1.1341-1(a)(1) of the Income Tax Regulations provides that ' 1341 applies if the taxpayer is entitled to a deduction of more than $3,000 because of the restoration to another of an item that was included in the taxpayer=s gross income for a prior taxable year (or years) under a claim of right.

Under the claim of right doctrine, a taxpayer that receives an amount under a claim of right without restriction on disposition must include the amount in gross income in the taxable year received, notwithstanding that the taxpayer=s right to retain the amount received may be uncertain and the taxpayer subsequently may be required to restore the amount to the rightful owner. *North American Oil Consol. v. Burnet*, 286 U.S. 417, 424 (1932).

In *United States v. Lewis*, 340 U.S. 590 (1951), the Supreme Court concluded that a taxpayer who was required under the claim of right doctrine to include a bonus in income in the taxable year received, and who had to repay part of the bonus in a later year, could not amend his tax return for the earlier year. The taxpayer=s only remedy was to deduct the amount repaid in the taxable year in which the taxpayer restored it to the payor. The Court followed the principle that income is properly reported under the claim of right doctrine in the year received, consistent with a tax system based on annual rather than transactional accounting. *See Burnet v. Sanford & Brooks Co.*, 282 U.S. 359, 364, 365 (1931).

The application of the claim of right doctrine may result in an inequity when, because of changes in tax rates or other circumstances, the tax increase resulting from the income inclusion in the earlier year exceeds the tax decrease that results from the deduction in the later year. Congress enacted ' 1341 to ameliorate this inequity in cases such as *Lewis,* in which a taxpayer receives an amount that it is required in a later taxable year to restore or repay to another claimant. *See* S. Rep. No. 1622, 83d Cong. 2d Sess. 118 (1954)

(AUnder present law if a taxpayer is obligated to *repay* amounts which he had *received* in a prior year and included in income because it appeared that he had an unrestricted right to such amounts, he may take a deduction in the year of restitution@) (emphasis added); H.R. Rep. No. 1337, 83d Cong. 2d Sess. 86 (1954) (same).

Section 1341(a)(2) requires that it be established after the close of the taxable year or years that the taxpayer did not have an unrestricted right to the item of gross income or portion thereof. To satisfy this test the taxpayer must repay or restore the item or portion of the item to another claimant. Section 1.1341-1(a)(1); *see also Chernin v. United States*, 149 F.3d 805 (8th Cir. 1998) (relying on a Alegislative history [that] is replete with references to repayment, restoration, and restitution@); S. Rep. No. 1622, 83d Cong. 2d Sess. at 118; H.R. Rep. No. 1337, 83d Cong. 2d Sess. at 86.

For purposes of ' 1341, to restore an item included in income, the repayment must arise out of the same circumstances, terms, and conditions as the original payment of the item to the taxpayer. *Griffiths v. United States*, 54 Fed. Cl. 198 (2002). The fact that the amount of the repayment bears no relationship to the amount included in income indicates that the repayment does not arise from the same or specific circumstances, terms, and conditions as the original transaction. *Bailey v. Commissioner*, 756 F.2d 44 (6th Cir. 1985); *Uhlenbrock v. Commissioner*, 67 T.C. 818 (1977).

In both *Situation 1* and *Situation 2*, the environmental remediation costs *N* incurs in 2004 do not qualify for treatment under § 1341(a). *N* did not include an item in gross income that *N* is repaying or restoring in a later year. In these situations, the item of gross income for purposes of ' 1341(a) is the proceeds received from the sale of *N*=s products from 1950 to 1979. *See* Rev. Rul. 72-28, 1972-1 C.B. 269. During 1950 to 1979, *N* had an unrestricted right to the proceeds received from the sale of *N*=s products during those years. In 2004, *N*=s right to the sales proceeds received during 1950 to 1979 remains unrestricted. *N*=s payment of the environmental remediation costs does not restore in a later taxable year any portion of the proceeds received from the original sale of *N*=s products in 1950 through 1979. Moreover, *N*>s obligation to incur the environmental remediation costs does not arise from the same or specific circumstances, terms, or conditions as the original sale of *N*=s products in 1950 to 1979. The amount of *N*=s environmental remediation costs bears no relation to the amount of proceeds received from the sale of *N*=s products in 1950 to 1979. Accordingly, *N*=s payment of environmental remediation costs in 2004 is not a repayment or restoration of an item included in gross income. *N*=s environmental remediation costs do not satisfy the repayment or restoration requirement of ' 1341(a)(2).

Section 1341(a)(2) also requires, as a prerequisite to ' 1341 treatment, that a

deduction must be allowable to the taxpayer for the repayment or restoration of the item included in income. Section 1341 itself provides no right to a deduction. Instead, the deduction must be allowable under another provision of the Code. Section 1.1341-1(a)(1); *Wood v. United States*, 863 F.2d 417, 420 (5th Cir. 1989); *MidAmerican Energy Co. v. Commissioner*, 114 T.C. 570, 583(2000), *aff=d*, 271 F.3d 740 (8th Cir. 2001).

Inventory costs under ' 263A are recovered through cost of goods sold when the inventory is sold. Section 1.263A-1(c)(4). Costs of goods sold, or inventory costs, are not deductions but are properly treated as adjustments to gross income. Section 1.61-3(a). Environmental remediation costs incurred by reason of a production activity must be included in inventory costs. *See* Rev. Rul. 2004-18, 2004-8 I.R.B. (clarifying Rev. Rul. 94-38, 1994-1 C.B. 35); ' 1.263A-1(e)(3). Thus, under ' 263A, *N*=s environmental remediation costs are inventory costs, not deductions. Furthermore, in *Situation 2*, because the environmental remediation costs *N* incurs in 2004 would have been accounted for under *N*=s method of accounting as inventory costs in 1950 through 1979 if incurred in those earlier years, the costs are properly treated as inventory costs under *N*=s method of accounting when incurred in 2004. Therefore, *N*=s environmental remediation costs do not qualify for treatment under ' 1341 because the costs are inventory costs and do not satisfy the deduction requirement of § 1341(a)(2).

Section 1341(b)(2) provides that ' 1341(a) does not apply to any deduction allowable with respect to an item included in gross income by reason of the sale or other disposition of the taxpayer=s stock in trade (or other property of a kind that would have been included in the taxpayer=s inventory if on hand at the close of the prior taxable year) or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business. Thus, even if *N*=s environmental remediation costs constituted deductible expenses rather than inventory costs recovered through cost of goods sold, ' 1341(a) would not apply. *N*=s environmental remediation costs are a consequence of the manufacture and sale of *N*=s products and, if not an inventory cost, would be deductible as an ordinary and necessary business expense of selling *N*=s products. Accordingly, in both *Situations 1* and *2*, the environmental remediation costs would be allowable with respect to an item that is included in gross income by reason of the sale of *N*=s products and would not be eligible for ' 1341(a) treatment by reason of ' 1341(b)(2).

HOLDING

Amounts paid or incurred in the current taxable year to remediate environmental contamination that occurred in prior taxable years do not qualify for treatment under ' 1341.

DRAFTING INFORMATION

The principal author of this revenue ruling is Forest Boone of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue ruling, contact Mr. Boone at 202-622-4960 (not a toll-free call).

Part I

Section 263A.BCapitalization and Inclusion in Inventory Costs of Certain Expenses

26 CFR 1.263A-1: Uniform capitalization of costs.
(Also ' 162.)

Rev. Rul. 2004-18

ISSUE

Are costs incurred to clean up land that a taxpayer contaminated with hazardous waste by the operation of the taxpayer=s manufacturing plant includible in inventory costs under ' 263A of the Internal Revenue Code?

FACTS

X, a corporation using an accrual method of accounting, owns and operates a manufacturing plant that produces property that is inventory in *X*=s hands. *X*'s manufacturing operations discharge hazardous waste. In the past, *X* buried this waste on portions of *X*=s land. The land was not contaminated by hazardous waste when purchased by *X*.

In order to comply with applicable federal, state, and local environmental requirements, *X* incurs costs (within the meaning of ' 461(h)) to remediate the soil and groundwater that had been contaminated by the hazardous waste, and to establish an appropriate system for the continued monitoring of the groundwater to ensure that the remediation removes all hazardous waste. The costs *X* incurs are not research and experimental expenditures within the meaning of ' 174 or environmental management policy costs. The soil remediation and groundwater treatment restores *X*'s land to essentially the same physical condition that existed prior to the contamination. During and after the remediation and treatment, *X* continues to use the land and operate the plant in the same manner as *X* did prior to the cleanup except that *X* disposes of any hazardous waste in compliance with environmental requirements.

LAW

Section 263A(a) provides that the direct costs and indirect costs properly allocable to property that is inventory in the hands of the taxpayer shall be included in inventory costs.

Section 1.263A-1(a)(3)(ii) of the Income Tax Regulations provides, in part, that taxpayers that produce tangible personal property must capitalize (1) all direct costs of

producing the property, and (2) the property=s allocable share of indirect costs.

Section 1.263A-1(e)(3)(i) provides, in part, that indirect costs are properly allocable to property produced when the costs directly benefit or are incurred by reason of the performance of production activities. Cost recovery, production facility repair and maintenance costs, and scrap and spoilage costs, such as waste removal costs, are examples of indirect costs that must be capitalized to the extent the costs are properly allocable to produced property. See ' 1.263A-1(e)(3)(ii) (I), (O) and (Q).

Section 1.263A-1(e)(4)(iv)(I) provides that costs incurred for environmental management policy generally are not allocated to production or resale activities (except to the extent that the costs of any system or procedure benefit a particular production or resale activity).

Section 1.263A-1(c)(2)(ii) provides that the amount of any cost required to be capitalized under ' 263A may not be included in inventory or charged to capital account or basis before the taxable year during which the amount is incurred within the meaning of ' 1.446-1(c)(1)(ii). Pursuant to ' 461(h), in determining whether an accrual method taxpayer has incurred an amount for any item during the taxable year, the all events test shall not be treated as met any earlier than when economic performance occurs.

Section 1.263A-2(a)(3)(i) provides that any cost required to be capitalized by ' 263A must be capitalized regardless of whether the cost was incurred before, during, or after production.

Rev. Rul. 94-38, 1994-1 C.B. 35, analyzes whether costs incurred to clean up land and to treat groundwater that a taxpayer contaminated with hazardous waste from the taxpayer=s manufacturing business are capital expenditures. The ruling holds that the costs to clean up land used in the taxpayer=s manufacturing process and to treat groundwater are not capital expenditures because these costs do not prolong the useful life of the land or adapt the land to a new or different use. Therefore, costs incurred to clean up land and to treat groundwater that a taxpayer contaminated with hazardous waste from the taxpayer=s business are deductible by the taxpayer as business expenses under ' 162. Costs properly allocable to constructing groundwater treatment facilities, however, are capital expenditures under ' 263.

Rev. Rul. 98-25, 1998-1 C.B. 998, holds that costs incurred to replace underground storage tanks containing waste by-products under the circumstances in the ruling are not capital expenditures under ' 263, but are ordinary and necessary expenses under ' 162.

ANALYSIS

The discussion in Rev. Rul. 94-38 of *Plainfield-Union Water Co. v. Commissioner*, 39 T.C. 333 (1962), *nonacq*., 1964-2 C.B. 8, demonstrates that the revenue ruling was intended to address whether the costs to clean up the land and to treat the groundwater are capital expenditures that must be capitalized into the basis of the land under ' 263(a) or whether the costs are ordinary and necessary repair expenses under ' 162. Rev. Rul. 94-38 does not address the treatment of these costs as inventory costs under ' 263A. Similarly, Rev. Rul. 98-25 does not address whether amounts incurred to replace underground storage tanks must be included in inventory costs under ' 263A.

The holding of Rev. Rul. 94-38 that the costs to construct a groundwater treatment facility must be capitalized under ' ' 263(a) and 263A rather than deducted under ' 162 demonstrates the distinction between capital expenditures and costs that are more in the nature of repairs than capital improvements. As with other types of deductible business costs, such as labor costs, taxes, rent, and supplies, once repair costs are determined to be deductible under ' 162, a taxpayer with inventories must still apply the rules of ' 263A to determine whether the repair costs must be included in inventory. Section 1.263A-1(e)(3). In addition, if repair costs must be capitalized under ' ' 263(a) and 263A to a depreciable asset, a taxpayer with inventories must still apply the rules of ' 263A to determine whether the depreciation expense must be included in inventory. Section 1.263A-1(e)(3)(ii)(I).

In this situation, *X* incurs environmental remediation costs to clean up land that was contaminated as part of the ordinary business operations of *X*=s manufacturing of inventory. *X*=s environmental remediation costs are incurred by reason of *X*=s production activities within the meaning of ' 1.263A-1(e)(3)(i). The costs are properly allocable to property produced by *X* that is inventory in *X*=s hands under ' 1.263A-1(e)(3)(i). Accordingly, *X* must capitalize the otherwise deductible environmental remediation costs by including the costs in inventory costs in accordance with ' 1.263A-1(c)(3). Similarly, costs incurred to replace underground storage tanks and depreciation cost recoveries of the groundwater treatment facility must be included in inventory costs to the extent properly allocable to inventory.

HOLDING

Environmental remediation costs are subject to capitalization under ' 263A. Therefore, costs incurred (within the meaning of ' 461(h) and ' 1.263A-1(c)(2)(ii)) to clean up land that a taxpayer contaminated with hazardous waste by the operation of the taxpayer=s manufacturing plant must be included in inventory costs under ' 263A.

TRANSITION RULE

This paragraph applies to costs that would have been properly deducted in the taxable

year but for the requirement to capitalize the costs to inventory under § 263A, and for which the taxpayer's method of accounting was to deduct the costs. The Internal Revenue Service will not challenge the treatment of environmental remediation costs to which this paragraph applies as deductible expenses rather than as costs properly capitalized to inventory under § 263A in any taxable year ending on or before February 6, 2004. Therefore, the treatment of environmental remediation costs to which this paragraph applies as amounts properly capitalized to inventory under § 263A will not be raised as an issue in any taxable year ending on or before February 6, 2004, and, if the treatment of such environmental remediation costs as deductible expenses rather than as amounts properly capitalized to inventory under § 263A has already been raised as an issue in examination or before Appeals or the Tax Court in a taxable year ending on or before February 6, 2004, the issue will not be further pursued. The Service will not impose penalties on taxpayers or preparers for treating environmental remediation costs to which this paragraph applies as deductible expenses rather than as costs properly capitalized to inventory under § 263A in taxable years ending on or before February 6, 2004.

CHANGE IN METHOD OF ACCOUNTING

A taxpayer using a method of accounting that does not comply with this revenue ruling is using an impermissible method of accounting. Any change in a taxpayer's treatment of environmental remediation costs to conform with this revenue ruling is a change in method of accounting to which the provisions of ' ' 446 and 481 and the regulations thereunder apply. A taxpayer changing its method of accounting to comply with this revenue ruling must file a Form 3115 in accordance with the automatic change in method of accounting provisions of Rev. Proc. 2002-9, 2002-1 C.B. 327, as amplified, clarified and modified by Rev. Proc. 2002-54, 2002-2 C.B. 432, and Rev. Proc. 2002-19, 2002-1 C.B. 696, with the following modifications: (1) the scope limitations in section 4.02 of Rev. Proc. 2002-9 do not apply to a taxpayer that wants to make the change for its first taxable year ending after February 6, 2004; and (2) a taxpayer that files a Form 3115 in accordance with this revenue ruling to make the change in method of accounting for its first taxable year ending after February 6, 2004, may effect the change using either a ' 481(a) adjustment as provided in sections 5.03 and 5.04 of Rev. Proc. 2002-9 or a cut-off method. For purposes of Line 1a of Form 3115 (revised December 2003), the designated number for the automatic accounting method change authorized by this revenue ruling is "77." A taxpayer making the automatic change in method of accounting authorized by this revenue ruling and another automatic change in method of accounting under § 263A for the same taxable year may file one Form 3115 to make both changes, but must comply with the ordering rules of § 1.263A-7(b)(2) and must enter the automatic accounting method change numbers for both changes on Line 1a of Form 3115 (revised December 2003).

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 98-25 and Rev. Rul. 94-38 are clarified by providing that the otherwise

deductible amounts at issue in Rev. Rul. 98-25 and Rev. Rul. 94-38 are subject to capitalization to inventory under ' 263A.

Rev. Proc. 2002-9 is modified and amplified to include in the APPENDIX the automatic change provided in this revenue ruling.

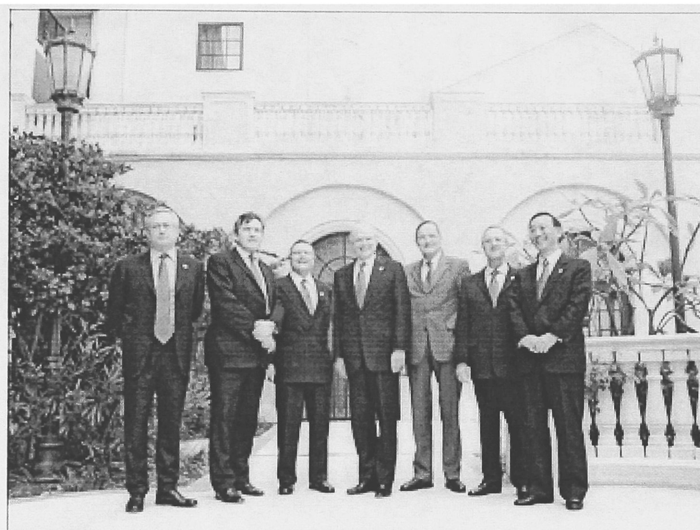
DRAFTING INFORMATION

The principal author of this revenue ruling is John Moriarty of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue ruling, contact Mr. Moriarty at 202-622-4930 (not a toll-free call).

FROM THE OFFICE OF PUBLIC AFFAIRS

February 8, 2004
JS-1154

Secretary John Snow hosts G-7 Finance Ministers



Secretary John Snow hosts G-7 Finance Ministers

Media Contact Secretary John Snow hosts G-7 Finance Ministers

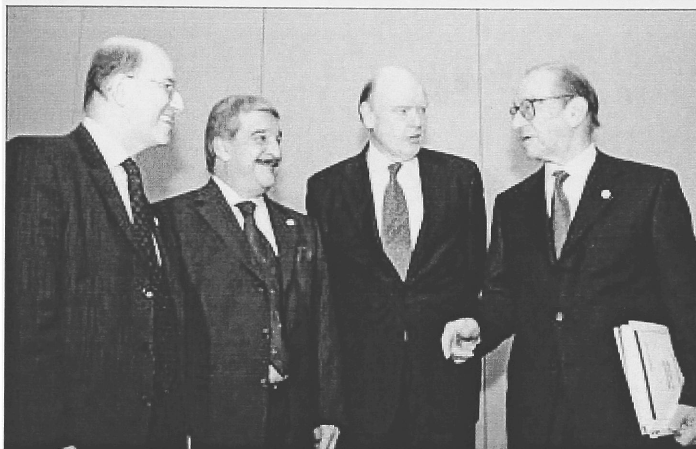
High Resolution Image

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 7, 2004
JS-1155

Photo: Treasury Secretary John Snow hosts the G-7 event at Boca Raton, FL.



(Left to Right) Sinan Al-Shabibi, Governor, Central Bank of Iraq, Kamel Al-Gailani Minister of Finance, Secretary John Snow and Chairman Alan Greenspan.

Media Contact

All media queries should be directed to the
Press Office at (202) 622-2960.
Only call this number if you are a member of the media.

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PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 7, 2004
JS-1156

Photo: Treasury Secretary John Snow greets Minister of Finance Sadakazu Tanigaki of Japan at the G7 conference held in Boca Raton, FL.

Media Contact

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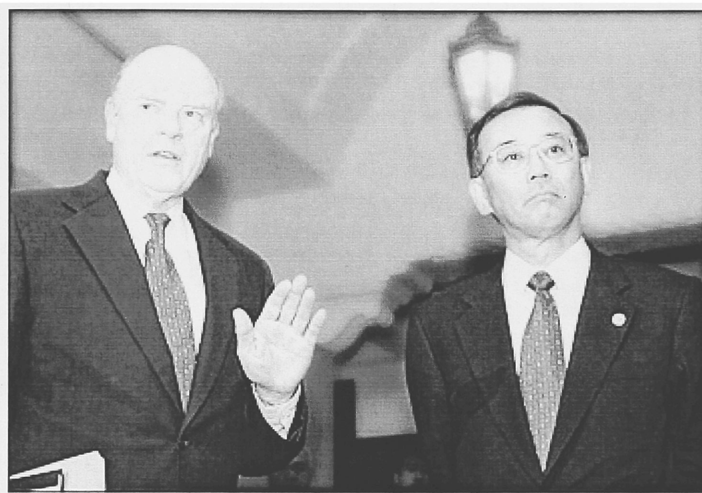
PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 7, 2004
JS-1157

Photo: Treasury Secretary John Snow greets Minister of Finance Sadakazu Tanigaki of Japan at the G7 conference held in Boca Raton, FL.



Media Contact

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PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 7, 2004
JS-1158

Statement of G-7 Finance Ministers and Central Bank Governors

The global economic recovery has strengthened significantly since our meeting in Dubai and risks have diminished. Growth projections for 2004 have been revised upward to their highest in three years. Fiscal and monetary policies have helped bring about these welcome changes.

Yet much more remains to be done. The pace of growth among our economies remains uneven. In our Agenda for Growth initiative, we emphasize supply-side structural policies that increase flexibility and raise productivity growth and employment. Today we released a progress report on our Agenda for Growth. This Agenda and sound fiscal policies over the medium-term are key to addressing global current account imbalances. We outlined strategies for sustained medium-term fiscal consolidation as economies recover. International trade is vital; we call for further efforts and for countries to take the steps to resume the Doha Round, which is pivotal to global growth and the alleviation of world poverty.

We reaffirm that exchange rates should reflect economic fundamentals. Excess volatility and disorderly movements in exchange rates are undesirable for economic growth. We continue to monitor exchange markets closely and cooperate as appropriate. In this context, we emphasize that more flexibility in exchange rates is desirable for major countries or economic areas that lack such flexibility to promote smooth and widespread adjustments in the international financial system, based on market mechanisms.

To combat terrorist financing, we urge all countries to strengthen their asset freezing regimes and to combat abuse of the informal financial sector and non-profit organizations. The IMF/World Bank should make permanent and comprehensive their assessments of countries' efforts to combat terrorism financing.

We are committed to further enhance transparency and supervisory standards in financial markets, in particular non-compliant off-shore centers.

We have a shared interest in seeing strengthened economic growth in the greater Middle East. We had a productive meeting with our counterparts from Afghanistan and Iraq. We welcome the completion of the currency exchange in Iraq and the removal of interest rate controls, and we look forward to the approval of the new central bank law. We welcome progress on reform and reconstruction in Afghanistan and the renewed efforts to collect revenues from the provinces. We call on others to join us in reducing the debt burdens of Iraq and Afghanistan. We welcome the plans of the IMF and the World Bank to provide financial and technical assistance to Iraq and Afghanistan.

The private sector plays a critical role in fighting global poverty and creating jobs in developing countries. We encourage the MDBs to work with governments to improve investment climates and provide more resources to support the private sector. Remittances are an important source of income for many developing economies. We aim to reduce the impediments that raise the cost of sending remittances. We reaffirm our commitment to fight global poverty and to help countries achieve the international development goals of the Millennium Declaration through our work on debt sustainability, aid effectiveness, absorption capacity, and financing facilities.

We discussed the progress in our efforts to reform the international financial

system, including improved surveillance, collective action clauses, limits on exceptional access, measuring results, and the use of other mechanisms, including grants, to avoid heavy debt burdens. We also discussed how to consolidate and build upon these reforms. We welcome the improvement in financial conditions, and the higher economic growth in many emerging market countries. We welcome the efforts by creditors and issuing countries to develop a code of conduct, which will be discussed in the G-20. We call on Argentina to implement policies in line with its IMF program. Argentina should engage constructively with its creditors to achieve a high participation rate in its restructuring.

Related Documents:

- Action Plan on Afghanistan
- Agenda for Growth Progress Report

Action Plan on Afghanistan
February 7, 2004

We met today with the Finance Minister and Central Bank Governor of Afghanistan, and we agreed on steps to support the Afghan Government's efforts to accelerate the creation of a dynamic market economy and to secure Afghanistan's future. The G-7 will continue to support the Government's development priorities in accordance with the National Development Framework. To that end, we will provide assistance that will produce visible and measurable results before June, as part of our long-term commitment to the country.

Human Capital: Afghanistan is making significant commitments to education and healthcare. The G-7 will continue to support these efforts to invest in Afghanistan's most valuable assets – its children – by building schools, training teachers, and providing textbooks. The G-7 will also continue to help the Government build additional health care facilities, and to support efforts to improve the status of women in Afghanistan.

Physical Capital: Improving the country's infrastructure, including its transport, electricity, and telecommunications systems, is a priority for the Afghan Government. We will help it reach its goals – such as a doubling of the percentage of paved roads in six years – by completing the Kandahar-Herat highway, and by supporting the efforts of international bodies to complete, by the end of 2004, roads they are constructing.

Private Sector Development: We will continue to support the Government's efforts to foster a climate where the private sector can flourish, including by providing assistance to the Government on trade and investment, and supporting microfinance lending. We urge bilateral and multilateral institutions to consider what support they can provide to those wanting to do business in and with Afghanistan, within their rules and Afghanistan's capacity.

Economic Governance: We will support the Government's efforts to ensure an adequate revenue base through improvements in provincial revenue collection, and to strengthen expenditure management, internal debt management systems and statistical capacity. We will provide technical assistance to support the Government's strengthening of key institutions and improvement of the civil service, and will also work with all creditors to ensure that Afghanistan's debt situation is sustainable, and with bilateral donors to provide as much assistance as possible in the form of grants.

Security and Rule of Law: The Government has noted the risks to private sector development and to the well-being of the Afghan people arising from weak security and rule of law. We will continue to support the Government in its efforts to address these problems, including through reforms to the police and legal systems; the disarmament, demobilization and reintegration of ex-combatants; and expanding security outside Kabul through the Provincial Reconstruction Teams. We recognize that opium production poses a major threat to security, economic growth and reconstruction in Afghanistan. We call upon the international community and the Afghan authorities to join together to eliminate opium production.

Finally, we pledge to provide support to Afghanistan over both the short and long term, and to help ensure the success of the international conference in March. We will increase our assistance, through bilateral and multilateral efforts, such as the Afghanistan Reconstruction Trust Fund.

Agenda for Growth
Progress Report
February 7, 2004

In September 2003, we adopted the Agenda for Growth initiative to focus our efforts on the need to undertake supply-side and structural policy changes to increase flexibility, raise productivity growth and employment, and achieve higher, sustained growth in our countries. Such reforms sometimes may entail short-term costs, but have proven critical to advancing long-term growth. We also committed to experience-sharing, to reviewing our results together, and to reporting on our progress. Our focus is on cooperation. Today, in Boca Raton, we reviewed our accomplishments thus far and outlined our future priorities. In this Progress Report, we list selected accomplishments since September 2003 -- one for each country -- and review upcoming reform plans.

Accomplishments since September. Germany enacted key elements of the reform Agenda 2010, including labor market measures that improve work incentives and further tax reduction. Canada completed the full implementation of its five-year, $100 billion tax reduction plan. Japan formulated a pension reform plan in December 2003 with a view to securing long-term sustainability of the pension system, and is preparing for legislation to implement the reform. France is implementing key provisions of its pension reform law that significantly improves the sustainability of its public finances. The United Kingdom announced new measures to help small business raise finance and to help promote a culture of enterprise, and to improve access to its R&D tax credit. Tax rate cuts in the United States worked their way through the economy to promote record growth. Italy's recent labor market reforms entered fully into force in October, contributing to the further reduction in the unemployment rate.

Upcoming Reform Plans. Our governments remain committed to pursuing additional pro-growth policies. The United States plans to spur saving by creating lifetime and retirement savings accounts and reducing the structural budget deficit, and to support job creation by making health care more affordable and pressing for tort reform. In an effort to raise productivity, the United Kingdom is targeting reductions in enterprise regulatory requirements including a collaborative initiative on regulatory reform across the EU over the next two years, establishing a long-term strategy for funding innovation and scientific research, and extended skills training programs. While continuing its steady reduction in the debt-to-GDP ratio, Canada will provide municipalities with the resources they need for infrastructure investment by exempting them from the Goods and Services Tax they now pay (worth $7 billion over the next decade) and examining other fiscal mechanisms to provide further predictable funding. Italy expects to push forward with its pension and corporate tax reform, including tax exemptions on dividends and capital gains, in 2004. France plans to advance health care reforms this year, while continuing to press for fewer labor market constraints. Japan will work on further fiscal expenditure and revenue reforms, including in social security, and will continue to address financial sector reforms. Pension and tax code reform remain key priorities in Germany, combined with further improvements in the framework for innovation.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 7, 2004
JS-1159

Statement by U.S. Treasury Secretary John Snow following the G-7 Finance Ministers' Meeting Boca Raton, Florida, February 7, 2004

Good afternoon. I was extremely pleased to host my fellow G-7 Finance Ministers and Central Bank Governors in Florida this weekend.

The need for increased global growth was at the top of our agenda. We were all encouraged to see that the global economic recovery has accelerated since we met in Dubai in September. Economic stability is also improving, and risks have diminished. We welcomed these developments. We all depend on each other. Stronger global growth is in the U.S. interest, and of the G-7, and the world. We also recognize that more work is needed to ensure growth that is broad-based and sustainable, and is less reliant on a single engine.

We reaffirmed our commitment to the Agenda for Growth initiative launched last September. This initiative focuses on supply-side reforms to boost productivity, raise growth and employment, and thereby increase living standards. I refer you to the progress report that we released summarizing actions taken in each country and outlining next steps.

For our part, I was proud to report on what we have achieved in the United States since the Dubai meeting. Due to the President's economic leadership, the U.S. economy is in a strengthening recovery. The President's tax cuts have worked. They provided the stimulus that was necessary to turn the economic ship around and they are now encouraging and allowing for the economic growth that is continuing into the future.

- Economic growth in the second half of 2003 was the fastest since 1984;
- New home construction was the highest rate in almost 20 years;
- Homeownership levels are at historic highs;
- Manufacturing activity is increasing;
- Inflation and interest rates are low;
- Jobs are coming back;
- Unemployment claims both initial claims and continuing claims - are falling, indicating improvement in the labor market;
- There is more than three trillion dollars of growth in value in the markets.
- These economic indicators all point to the same conclusion: We are on a path to sustained economic growth. However, there is more to do. We are not, by any means, satisfied. We will keep working until every American who wants work can find a job.

I also discussed initiatives we will be pursuing in coming months. I detailed for my colleagues the commitments that President Bush has made to maximize growth and job creation, including spurring saving through changes to the tax system; making health care more affordable; working to prevent frivolous lawsuits from diverting money from job creation; streamlining regulations; preparing American workers for the demands of the 21st century job market; and working to make tax relief permanent, so that families and businesses alike can plan for the future.

I was also pleased to hear the details of others' efforts and their dedication to going further to increase labor and product market flexibility, boost productivity and raise employment. But words are not enough. Our actions will be the measure of success.

During our discussion, I reaffirmed our policy in support of a strong dollar. A strong

dollar is in the national interest. The relative values of currencies are best set in open, competitive markets.

Sound fiscal policies are also a key ingredient for sustained growth, and it will be important that we all reduce our budget deficits as our economies recover. I underscored to my colleagues that President Bush is serious about deficit reduction. If we stick to his strong, pro-growth economic policies and proposed measures for spending restraint, we expect to cut the deficit in half, to about 2 percent of GDP, over the next five years.

I want to turn now to Afghanistan and Iraq, another key item on our agenda here today. It was my pleasure to include representatives from these two countries in our deliberations. The economic revival of these nations is vital to their citizens and important to the war on terror. These impressive leaders are playing an extraordinarily important role, and we all commend their efforts. We took particular note of the completion of the currency exchange in Iraq - a vital step forward as well as the deregulation of interest rates and the increasing openness of the banking sector to foreign investment.

On Afghanistan, the G-7 took an important step in laying out an action plan aimed at helping to accelerate the creation of a functioning and sustainable market economy in a post-conflict country. Key steps are education, healthcare, infrastructure repair and construction, private sector development, improved revenue collection, and security sector reform. We each committed our support for the Afghan government with the goal of producing visible and measurable on-the-ground results before midyear. And, more broadly, we all agreed that we share an interest in strengthening economic growth and raising living standards in the greater Middle East.

Our commitment to combating terrorist financing continues. We agreed to a timetable of specific actions with measurable deadlines for this year to strengthen asset freezing regimes and combat abuse of the informal financial sector and non-profit organizations. We also called on the IMF and World Bank to assess compliance with the entire set of FATF recommendations on a permanent basis. We are extremely pleased with the extensive collaboration on this issue, which goes well beyond the G-7. We look forward to continuing this cooperative work to make it much harder for terrorist financiers to do business.

Turning to the poorest countries, I emphasized today that creating an environment that allows private businesses to flourish should be a higher priority on the development agenda. We all agreed that the World Bank and regional banks should work to improve investment climates and direct more resources to the private sector.

We focused on the flow of remittances, which are a tremendous source of capital flowing directly into the hands of consumers and households in the developing world. We agreed to work on reducing the roadblocks for people sending money back to their families. This means identifying and removing the barriers that slow the flow of remittances, make transactions expensive or encourage money to flow through informal channels. Improving access to financial services and infrastructure is particularly important. We in the United States have already been working closely with our key remittance partners, such as Mexico and the Philippines, to tackle these issues. I urged my counterparts to do what they can in this regard.

Looking at the international financial system more broadly, we took note of the progress made in the past year in advancing reform. Collective action clauses are taking hold as the market standard in external sovereign bond issues under New York law in external bond issues. Widespread use of these clauses will help increase predictability. We also took note of reforms implemented to limit exceptional access in the IMF, measure and account for results in the MDBs and shift to grants in the MDBs to help avoid building heavy debt burdens.

We recognize the critical importance of Argentina to live up to its IMF commitments and urge them to move forward on their needed reforms.

Thank you.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 9, 2004
JS-1160

Treasury Secretary John W. Snow
Remarks to Cuban American Leaders
Miami, FL

Thank you; it's great to be here in Miami. I've been at the G-7 summit this weekend just a few miles north in Boca Raton, and we had a very productive meeting. I was pleased to be able to report to that group some very good economic news from the U.S., and I'd like to share that news with you as well.

But first, there is another area of economic policy that I really want to talk to you about today, and that's the United States' policy on Cuba. Let me be perfectly clear and candid: The President loathes what the Cuban government has done to Cuba. Castro's regime has crushed freedom and has held Cuba back from its enormous potential as an economic power and a friend to the United States.

The President is, however, very dedicated to the people of Cuba, who long for freedom and have suffered so much under Castro. Because of his dedication to the people of Cuba, President Bush offered, in 2002, to ease U.S. bans on trade and travel... but only if the Cuban government held free and fair elections and allowed free speech and free enterprise.

Rather than take this opportunity to move toward a new day for the Cuban people, Castro was contemptuous in response to that offer. Instead, he followed with a new round of brutal oppression of the Cuban opposition that sickened all those who respect human life, dignity and freedom.

You know this better than anyone: Until Castro's reign is ended, any money that is spent in Cuba – for products or tourism – benefits only that oppressive government, not the hard-working people of Cuba. Any economic benefit is used not to benefit the Cuban people, but instead to perpetuate the regime's strangulation of its population.

That is why sanctions, especially on travel, are being vigorously enforced by the Bush administration, and why the President told Congress he would veto any attempt to weaken the prohibitions on travel and trade. As you know all too well, dollars spent at Cuban hotels go to the dictator's government coffers. That government in turn pays only a few measly pesos to the staff who work at those hotels.

We must not and we can not have American dollars lining Fidel Castro's pockets and those who would perpetuate his oppressive regime... and enforcement actions by the Department of the Treasury, along with the Department of Homeland Security (DHS), are making sure that does not happen.

Treasury's Office of Foreign Assets Control (OFAC) is working closely with Customs agents on inspecting all direct flights to Cuba at Miami, JFK and LAX. That's hundreds of aircraft and tens of thousands of passengers... and agents are being extremely meticulous.

OFAC has provided on-site training, specifically on Cuba embargo travel restrictions, to over 500 DHS Customs inspectors. We have accomplished this training on-site in Miami, Los Angeles and JFK, and are now expanding our training efforts to reach Customs inspectors stationed at U.S. Customs Preclearance Facilities in the Caribbean and Canada. We've already trained Preclearance

Customs staff in Bermuda, Nassau and Aruba. The training will assist inspectors in their efforts to detect illegal U.S. tourist travelers
to Cuba.

We are also providing training to Customs inspectors on a monthly basis at the Federal Law Enforcement Training Center in Brunswick, Georgia.

OFAC's Miami Office is working with the Coast Guard to provide Cuba travel embargo training for its personnel.

By increasing training and awareness of existing law, we are tightening the economic noose around the regime. We expect that this will result in an increase in OFAC civil penalties imposed.

Since October 10th, 264 cases have already been opened by OFAC's enforcement division for investigation of alleged travel to Cuba. Three cases have been referred for criminal investigation.

Also since the training and inspection efforts have intensified, at the direction of President Bush, nearly three hundred passengers have been denied travel after an examination revealed they did not qualify under any legitimate license category for travel to Cuba.

Stepped-up inspection efforts have also had a positive ripple-effect on our financial offensive. For example, using information gathered from these inspections, OFAC has been able to suspend licenses issued to two organizations previously authorized to engage in travel transactions allegedly related to humanitarian or religious activities in Cuba. OFAC is now investigating allegations that the licensees may have engaged in activities outside the scope of their licenses.

Homeland Security has assisted the OFAC sanctions program against Castro with almost 400 seizures of products like Cigars and alcohol... again, Cuban profit on these items is Castro's profit, not the Cuban people's, and that will not be tolerated by the United States government.

On March 24th, new OFAC rules eliminated the "people to people" educational license that had allowed educational travel unrelated to academic coursework. The license had increasingly been abused for trips that amounted to little more than tourist travel, thus undermining the intentions of the U.S. sanctions against Cuba. So we got rid of it. Because we're serious about enforcing the sanctions.

I'm pleased to announce to you, today, another enforcement action that is part of these rigorous efforts to choke off Castro's supply of dollars:

OFAC is identifying and blocking ten entities that it has determined are owned or controlled by the Government of Cuba or Cuban nationals. They include entities organized and located in Cuba as well as entities organized and located in Argentina, the Bahamas, Canada, Chile, the Netherlands, and England. Nine of the ten are travel companies specializing in Cuba travel and one is a forwarder of gift packages to Cuba.

As a result of today's action, all property of these entities that is in the possession of persons subject to U.S. jurisdiction is blocked and no persons subject to U.S. jurisdiction may engage in any transactions with these entities unless authorized by OFAC.

These companies have been providing easy access to Cuba to those U.S. individuals who chose to break the law. Today's action will put a stop to that, and a stop to another illegal pathway for U.S. dollars to Castro's wallet.

We're cracking down. We mean business. We're cutting off American dollars headed to Fidel Castro, period. At the same time, we're reaching out to the freedom-hungry people of Cuba.

While we will not tolerate illegal travel to Cuba, we sympathize with those desperate to travel here from Cuba. Because until Cuba is free, people will risk their lives to

come to these shores of freedom.

That's why President Bush's administration is dedicated to finding safe routes for Cubans who are fleeing Castro.

The President also established the Commission for Assistance to a Free Cuba. The purpose of that Commission, as the President said when he announced its creation, is to "plan for the happy day when Castro's regime is no more and democracy comes to the island."

The Commission will draw upon experts in our government to plan for Cuba's eventual transition for example, best practices on the establishment of democratic institutions; how to ensure a respect for human rights and rule of law; how to create the core institutions of a free economy; how to modernize infrastructure; and how to quickly meet basic needs in areas of health, education, housing, and human services.

President Bush is also breaking the information embargo that Cuban government has imposed on its own people. We're doing that by increasing the amount and expanding the distribution of printed material to Cuba, of Internet-based information inside of Cuba, and of AM-FM and shortwave radios for Cubans.

Radio and TV Marti are bringing the message of freedom to the Cuban people. Earlier this year, we launched a new satellite service to expand our reach to Cuba. On May 20th, we staged the historic flight of Commando Solo, an airborne transmission system that broke through Castro's jamming efforts. On that day, our President was honored to speak to the Cuban people in the native tongue.

Until the Cuban people are free, President Bush and his administration will do everything in our power to keep dollars out of Castro's pocket while extending the hand of freedom to the Cuban people.

Because we know that these efforts will lead us to a day when we will celebrate Cuba's freedom together. A day when we will see and embrace Dr. Oscar Elias Biscet, Martha Beatriz Roque, Oscar Espinosa Chepe, Leonardo Bruzon Avila, Juan Carolos Gonzalez Leyva... you know the names. They are in your hearts and prayers every day.

I look forward to that day of Cuban liberation, and dedicate myself and my office to speeding its arrival.

Before I leave here today, I want to share with you some good economic news that I hope is serving as inspiration to the leaders of the G-7 countries that I met with this weekend.

In recent months, it has become clear that President Bush's tax cuts did precisely what they were intended to do: unleash the economic potential of this great country. Our economic indicators are now positive, across the board. Homeownership is up, unemployment rates are heading down, GDP growth has been extremely strong, and jobs are being created.

As you know, this administration came to office when those indicators were not nearly as positive. The President inherited an economy that was in decline... one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

The President and his administration took these challenges seriously and we have made serious progress in changing the economic direction of this country.

As you've seen here in Florida – your economy is doing generally even better than the national economy – the President's tax cuts have worked. They provided the stimulus that was necessary to turn the economic ship around...and they are now encouraging and allowing for the economic growth that is continuing into the future.

- Economic growth in the second half of 2003 was the fastest since 1984;
- New home construction was the highest in almost 20 years;

- Homeownership levels are at historic highs;
- Manufacturing activity is increasing;
- Inflation and interest rates are low;
- Over a quarter million jobs were created in the last five months of 2003, and over 100,000 were created in the first month of 2004;
- Unemployment claims – both initial claims and continuing claims – are falling, indicating improvement in the labor market;
- And two weeks ago, the Dow closed at a 31-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: We are on a path to sustained economic growth.

However, there is more to do. We are not, by any means, satisfied. There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

We can encourage the creation of jobs by sticking to the President's six-point plan for growth.

That includes making health care more affordable and costs more predictable; passing tort reform measures to make the cost of doing business lower and less like Russian Roulette; passing an affordable, reliable energy supply; streamlining regulations and reporting requirements – particularly for small businesses, who create the majority of new jobs; opening new markets for American products; and enabling families and businesses to plan for the future with confidence by making the President's tax relief permanent.

I talked about all of these things before Congress last week, as part of the release of the President's budget. It's a good budget, one that speaks to our national priorities of both national and economic security.

The budget combines fiscal restraint with growth-friendly policies that will ultimately add up to deficit reduction.

That's where we are on our economy, and our economic policy right now... we're in very good shape, and credit goes to hard-working Americans like you.

Thank you for all you do for our country and our economy, and for the people of Cuba.

Thank you so much for having me here today.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 9, 2004
js-1161

Treasury Designates & Blocks 10 Entities for Cuban Embargo Violations

MIAMI--Today Treasury Secretary John Snow announced that Treasury's Office of Foreign Assets Control ("OFAC") is identifying ten entities, listed below, that it has determined are owned or controlled by the Government of Cuba or Cuban nationals. These ten include entities organized and located in Cuba as well as entities located in Argentina, the Bahamas, Canada, Chile, the Netherlands, and England. Nine of the ten are travel companies specializing in Cuba travel, and one is a gift forwarder to Cuba.

All property of these entities that is in the possession of persons subject to U.S. jurisdiction is blocked and no persons subject to U.S. jurisdiction may engage in any transactions with these entities unless authorized by OFAC.

OFAC is taking action today in furtherance of President Bush's October 2003 initiative to strengthen enforcement of U.S. laws prohibiting transactions related to travel to Cuba and to hasten the arrival of a new, free, democratic Cuba. The foreign travel companies identified today provide easy access to Cuba to those U.S. individuals who choose to break the law. Many of these entities use the Internet to advertise and sell Cuban tourism to the U.S. public. U.S. law enforcement officials have intercepted a number of unauthorized travelers whose tour packages were purchased through one of these entities.

ENTITIES PROPOSED FOR DESIGNATION

Cimex Companies (6):

1. 2904977 CANADA INC.
Montréal, Québec, Canada
(http://www.caribesol.ca)
2904977 CANADA INC., a.k.a. Caribe Sol, a.k.a. Havanatur Canada Inc., is a travel agency owned by Cimex, a holding company of the Government of Cuba.

2. CORPORACION CIMEX S.A.
Havana, Cuba (and all other locations worldwide)
(http://www.cimexweb.com)
CORPORACION CIMEX S.A., a.k.a. Cimex, a.k.a. Cimex Cuba, a.k.a. Comercio Interior, Mercado Exterior, has approximately 107 offices throughout Cuba. A holding company, CIMEX S.A., is owned by the Government of Cuba and owns travel service providers. It was organized to promote new products and services in Cuba.

3. HAVANATUR S.A.
Havana, Cuba (and other cities in Cuba)
(http://www.havanatur.cu)
HAVANATUR S.A. is the leading tour operator in Cuba, with offices throughout Cuba. Its corporate parent is CIMEX.

4. HAVANATUR S.A.
Buenos Aires, Argentina
HAVANATUR S.A. is a travel agency specializing in trips to Cuba. It is owned by Cimex.

5. HAVANATUR BAHAMAS LTD.
Nassau, Bahamas
HAVANATUR BAHAMAS LTD. is a travel agency specializing in trips to Cuba. It is controlled by the Government of Cuba.

6. HAVANATUR CHILE S.A.
Santiago, Chile
HAVANATUR CHILE S.A., f.k.a. Guamatur S.A., is a travel operation specializing in trips to Cuba. It is controlled by Cimex.

Cubanacan Companies (4):

1. LA COMPAÑÍA TIENDAS UNIVERSO S.A.
Cuba
(http://www.cuba-shop.net)
LA COMPAÑÍA TIENDAS UNIVERSO S.A, which is owned by the Cubanacan Group, operates the e-commerce portal CUBA-SHOP.NET.
Through CUBA-SHOP.NET, U.S. persons may purchase a wide range of products, including but not limited to televisions, refrigerators, ovens, food, perfume, cosmetics and bicycles for friends and family in Cuba. Prices are in U.S. dollars.

2. CUBANACAN GROUP
Havana, Cuba
CUBANACAN GROUP, owned by the Government of Cuba, is a tourism and trading business, hosting approximately 40% of all visitors to Cuba.

3. CUBANACAN INTERNATIONAL B.V.
Zevenhuizen, Netherlands
CUBANACAN INTERNATIONAL B.V. specializes in organizing trips and accommodations for travel to Cuba.

4. CUBANACAN U.K. LIMITED
London, England, United Kingdom
CUBANACAN U.K. LIMITED is a travel agency specializing in travel to Cuba and is a promoter and representative of CUBANACAN GROUP.

OFFICE OF FOREIGN ASSETS CONTROL
STATUS REPORT ON IMPLEMENTATION OF ENHANCED CUBA TRAVEL ENFORCEMENT

Date: February 9, 2004

On October 10, 2003, President Bush directed the Departments of Treasury and Homeland Security ("DHS") to step-up enforcement of Cuba embargo travel restrictions by increasing inspections of travelers and shipments to and from Cuba, and by targeting those who travel to Cuba illegally through third countries and by private vessel for illegal business or tourism purposes or to carry unlicensed currency to Cuba.

The Office of Foreign Assets Control ("OFAC") reports the following actions and progress to date to fully implement and enforce the President's initiative.

Inspection of Cuba Flights

- DHS committed Bureau of Customs and Border Patrol ("Customs") to inspecting up to 100% of direct flights at Miami, JFK and LAX for a 90-day period. After 90 days, the level of future inspections will be reviewed and evaluated.

- OFAC's staff in Miami, augmented by staff from Washington, worked hand-in-hand with Customs inspectors in Miami during the first 90-day period to provide daily post-October 10 coverage of direct charter flights that depart several times each day for Cuba.

- Since October 10, OFAC has participated with Customs to inspect the weekly

charter flights at LAX and JFK twice at each port and we are in direct communication with DHS as questions arise.

- Inspection Activity to Date:

569 aircraft with passengers destined for Cuba, mostly direct charter flights, were targeted for outbound inspection. Over **44,000** passengers were screened as they departed the United States for Cuba and over **50,915** passengers were screened on their return to the United States on charter flights.

275 travelers were denied travel on charter flights after examination revealed they did not qualify under any OFAC license category.

1007 aircraft with passengers returning to the United States from Cuba were targeted for inbound inspections. This number includes returning charter flights and other flights arriving in the United States from third countries. Over **50,915** passengers and crew were subjected to extensive examination.

376 OFAC-related seizures were accomplished, most of which related to the unlicensed importation of Cuban cigars and alcohol.

Training

- Since October 10, OFAC has provided on-site training on Cuba embargo travel restrictions to over **500** DHS Customs inspectors. We have accomplished this training on-site in Miami, Los Angeles and JFK, the ports of departure for direct charter flights, and we are now expanding our training efforts to reach Customs inspectors stationed at U.S. Customs Preclearance Facilities in the Caribbean and Canada. This training will assist inspectors in their efforts to detect illegal U.S. tourist travelers to Cuba. OFAC has already completed training in Bermuda, Nassau and Aruba. In the next few weeks, OFAC will provide training to inspectors at **6** Preclearance Facilities in Canada.

In addition to these training sessions, OFAC provides training to Customs inspectors on a monthly basis at the Federal Law Enforcement Training Center in Brunswick, GA.

OFAC's Miami Office is working with the Coast Guard to provide Cuba embargo travel training for its personnel.

OFAC fully expects that these training initiatives will result in a significant number of travel referrals from Customs to OFAC for civil penalties.

Travel Enforcement Investigations

Civil -

- **264** cases have been opened to date by OFAC's Enforcement Division for investigation of alleged post October 10, 2003, travel to Cuba.

Criminal

- **3** cases have been referred for criminal investigation by OFAC Enforcement directly to federal law enforcement agencies, primarily the Bureau of Immigration and Customs Enforcement. OFAC is working with special agents and Assistant U.S. Attorneys on a number of potential criminal cases.

- On December 4, 2003, OFAC hosted a highly successful meeting in Miami with the U.S. Attorney for the Southern District of Florida, Commander of the 7th U.S. Coast Guard District, DHS (ICE and Bureau of Customs and Border Patrol), and Department of Commerce, to coordinate efforts to implement the President's initiative. The U.S. Attorney voiced the support of his Office. It was agreed that working groups from participant agencies will meet quarterly, beginning in March

2004, to review promising criminal cases. The Commander, USCG 7th District, stated that his organization will (1) redraft the Security Zone Permit to capture the OFAC and Commerce licensing category of the applicant, and will (2) step-up their boarding of pleasure vessels going to and from Cuba. OFAC agreed to provide Cuba travel training to USCG personnel in South Florida and to implement a feedback program for Customs and USCG to report the status of Cuba travel cases those agencies refer to OFAC for civil penalties.

Penalties

• OFAC's Civil Penalties Division plans to expedite action on those violations occurring after the President's Rose Garden directive to increase enforcement while continuing to issue penalties on currently ongoing cases.

-- OFAC's Civil Penalties Division currently has a docket of nearly 2,000 actions relating to Cuban embargo violations, the majority of which will likely result in monetary penalties paid to OFAC.

• Increased Initiation of New Penalty Actions - Since the President's announcement on October 10th, the Civil Penalties Division has accelerated the issuance of Prepenalty Notices initiating OFAC's civil penalty cases. By the end of November, all prepenalty notices in the pipeline were issued. Between October 10 and November 30, 2003, OFAC issued a total of approximately **348** new notices opening penalty actions.

• Implementation of Expedited Penalty Process - OFAC's Civil Penalties Division has implemented an expedited civil penalty process. For all post-Rose Garden announcement violations detected by DHS and referred to OFAC, OFAC's Civil Penalties Division will initiate appropriate civil penalty action within 60 days of the division's receipt of DHS' evidence of violation. Given the cumulative effect of the enhanced multi-agency enforcement strategy, we anticipate that at least initially an increase of cases by several orders of magnitude will be received in the Civil Penalties Division.

-- Major Case Squad Set Up for Cuban Commercial Cases – OFAC's Civil Penalties Division has set up a Major Case Squad targeting Cuban commercial cases in response to the President's Rose Garden directive for increased Cuban embargo enforcement. The Major Case Squad identified cases awaiting OFAC Civil Penalties Division action against banks, companies and other entities involved in commerce with Cuba. The Squad has contacted more than **60** violators and informed the majority of them of OFAC's pending penalty actions against them. Settlements totaling nearly **$200,000** have already been reached in **20** of the Major Cases.

-- OFAC's Civil Penalties Division publishes details of penalty settlements and assessments on OFAC's website. This information is updated each month. Penalties settled by and assessed against Cuban travel ban violators appear in the aggregate for informational purposes on the website.

• Administrative Law Judges OFAC now has 3 ALJs in place to hear civil penalty cases and the ALJs have begun issuing orders of hearing to violators. To date, OFAC has initiated action in cases by forwarding them to the 3 ALJs residing at the Justice Department and the Federal Mine Safety and Health Commission. Twelve cases are on the ALJs' docket as the balance has settled their cases with OFAC with penalty payments. One hundred eleven violators have been given acknowledgments of timely hearing requests along with advisories that orders instituting proceedings before the ALJs will be forthcoming in short order absent settlement of the case.

Of these 111 ALJ hearing-noticed cases, 63 violators have already sent in settlement payments with the deadline to pay in the other cases to run in 2 weeks. Additional settlements are expected.

Other OFAC Actions

• Licensing Actions –

- OFAC Licensing and Enforcement Divisions have established internal procedures to quickly suspend and investigate allegations of abuse of licenses issued to

humanitarian and religious organizations.

- Using information derived from charter flight inspections, OFAC has suspended licenses issued to **2** organizations previously authorized to engage in travel transactions related to humanitarian or religious activities in Cuba. OFAC is investigating allegations that the licensees may have engaged in activities outside the scope of their licenses. Four other organizational licenses are under review for possible suspension and investigation.

OFAC has taken action to limit the number of travel days in Cuba for licenses issued for humanitarian purposes, such as for the delivery of donated goods in Cuba.

• Regulatory / Policy Changes:

- OFAC is working with the State Department to review the current authorization which allows licensed travelers to import up to $100 worth of Cuban origin goods, including cigars and rum, as accompanied baggage. A revocation of this authorization would result in a significant decrease in U.S. dollars going directly to the state-owned tobacco and alcohol industry. Revocation would also serve to reinforce the seriousness of the U.S. Government's Cuba travel enforcement efforts.

Public Support

• Calls are regularly received at the OFAC hotline in Miami at **(305) 810-5170** to report embargo violations.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 9, 2004
JS-1162

Operation Balkan Vice III: TREASURY DESIGNATION OF Thirteen Individuals Obstructing the Dayton Peace Accords in Bosnia

Treasury Secretary John Snow announced today that Treasury's Office of Foreign Assets Control designated thirteen individuals under the Western Balkans Executive Order 13219, as amended by Executive Order 13304. Today's designation will allow the U.S. Treasury to block the assets in the U.S. of these individuals and to prohibit financial transactions with them by U.S. persons.

The 13 individuals were designated for obstructing, or the risk they pose for obstructing, or support for obstructing the Ohrid Framework Agreement of 2001 relating to Macedonia, and the Dayton Accords, including the decisions of the High Representative, relating to Bosnia and Herzegovina, or for assisting or supporting persons, or for having acted or purported to act on behalf of persons, designated pursuant to the order.

Those designated today were Dragan Basevic, Beljko Borovcanin, Samojko Djorda, Ljuban Ecim, Avdyl Jakupi, Radomir Kojic, Tomislav Kovac, Predrag Kujundzic, Milovan Marijanovic, Ivan Sarac, Mirko Saravic, Xhezair Shaqiri, and Menduh Thaci.

In a parallel action, at a news conference at 1 p.m. (7 a.m. EST) in Sarajevo, Bosnia and Herzegovina, Paddy Ashdown, the High Representative and EU Special Representative to Bosnia and Herzegovina, announced the blocking of the assets of 10 of the individuals in Bosnia and Herzegovina, the removal of three individuals from their positions as police officers and the removal of Mirko Sarovic from his position as vice president of the Serb Democratic Party.

Information available to the U.S. government indicates that, among other sanctioned activities, seven of these persons – Dragan Basevic, Beljko Borovcanin, Samojko Djorda, Ljuban Ecim, Tomislav Kovac, Ivan Sarac, and Mirko Sarovic – have used their positions in public office for the benefit of Milovan Bjelica, a person designated pursuant to E.O. 13219. Two of these persons – Radomir Kojic and Milovan Marijanovic – own or control commercial businesses suspected of providing support to persons indicted for war crimes (PIFWC's) by the International Criminal Tribunal for the former Yugoslavia or other persons designated pursuant to Executive Order 13219. Four of these persons – Avdyl Jakupi, Predrag Kujundzic, Xhezair Shaqiri, and Menduh Thaci – are leaders of armed militant groups opposed to the United Nations efforts to establish peace in Bosnia and Herzegovina.

Under Executive Order 13219, the President of the United States exercised his statutory authority to declare a national emergency in response to the unusual and extraordinary threat to national security and foreign policy of the U.S. by persons engaged in, or assisting, sponsoring, or supporting acts of obstructing implementation of the Dayton Peace Accords in Bosnia.

The United States has a vital interest in assuring peace and stability in Europe. In the Western Balkans, the U.S. is engaged, together with NATO Allies, the Organization for Security and Cooperation in Europe, UN missions, the EU, and other international organizations in an effort to achieve peace, stability, reconciliation, and democratic development and to facilitate the region's integration into the European mainstream. The U.S. views full implementation of the Dayton Peace Accords in Bosnia as critical to these efforts.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 10, 2004
JS-1163

**Statement of Samuel W. Bodman,
Nominee to be Deputy Secretary of the Treasury,
to the Senate Committee on Finance**

Mr. Chairman, Senator Baucus, Members of the Committee, thank you for the opportunity to appear before you today. I am honored to be President Bush's nominee to serve as Deputy Secretary of the Treasury Department, and I am most grateful to Secretary Snow for his confidence and support. As Deputy Secretary of the Commerce Department, I have had the privilege to serve President Bush and the American people since 2001. In that position, I've had the good fortune to work closely with several of you, and I look forward to what I know will be a productive relationship with this Committee.

I am most pleased that my wife, Diane, is here with me. I am the proud father of five children and eight grandchildren, and I'm blessed to have their continued support.

I was born in Chicago and raised in a small Illinois community, but I spent most of my adult life in Massachusetts. I went to Boston as an MIT graduate student and ended up staying for 40 years. I started out my career as a professor of chemical engineering at MIT In 1970, I joined a then-fledgling investment firm called Fidelity Investments. During my seventeen years there, the last ten as president, I helped orchestrate the transformation of a small company into one of the nation's largest financial service enterprises.

Following my time at Fidelity, I spent fifteen years serving as Chairman and CEO of Cabot Corporation, a specialty chemical manufacturer and one of Boston's oldest industrial companies. Operating 45 manufacturing plants in 25 countries, my colleagues and I faced many of the challenges that confront American companies in today's global marketplace – from international trade, to technology integration, to safety and security.

Three years ago, I resigned my job at Cabot; and Diane and I moved to Washington so that I might serve as Deputy Secretary of Commerce. Collectively, my experiences have instilled in me a strong belief in the power of the American free enterprise system, the engine of innovation, productivity, and job creation that drives our nation forward. And my time in Washington has reinforced my belief that government does have a crucial role to play in maintaining our economic health. As President Bush has said many times, government does not create wealth; the private sector does that. But government must create an environment that encourages the entrepreneur, that allows companies to plan, that provides the flexibility necessary to create and grow, and sometimes, to fail and start over.

It has been my privilege to work with the fine men and women of the Commerce Department to advance this vision for government. Under Secretary Evans's leadership, we have worked hard to open markets around the world, to promote free and fair trade, and to protect intellectual property. We have saved lives, homes, and businesses with more accurate and timely severe weather forecasts. We have promoted economic development and job growth throughout this nation. And, we have strengthened the management of our programs and Department.

There is more work to be done, and that's why I am so pleased that President Bush has extended the opportunity for me to continue my public service at the Treasury Department. The Treasury is at the forefront of many critical policy challenges: stopping the flow of funds to terrorists around the world; reforming and modernizing

the IRS; and ensuring that our current economic momentum translates into lasting prosperity for our citizens.

I'm proud to be afforded the great opportunity to serve the American people with President Bush, Secretary Evans, Secretary Snow, and now this Committee. With that, I would be pleased to take any questions that you may have.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 10, 2004
JS-1164

Secretary John W. Snow's Remarks to Tampa Business Leaders
Tampa FL

Thank you; it's great to be here in Florida.

This is a state that is leading the way, economically, serving as an example to follow for other states.

Generally speaking, you are out-performing the nation overall… in spite of the fact that a major industry in this state – tourism – was so deeply impacted by the terrorist attacks on our country in September of 2001.

That's one of the reasons why it is so impressive that your unemployment rate was down to 4.7 in December – that's the lowest since July of 2001 and well below the national rate.

It is also impressive that your total personal income is on the rise.

And even your international sector, which was hard hit by the woes of its key overseas trading partners, is showing some life. Total international merchandise trade rose by more than three percent in the third quarter of last year.

You're doing well, and your business community deserves credit for this economic growth. Florida's entrepreneurs are showing what the American free market can do when its potential is unleashed.

Unleashing our economic potential was the driving idea behind President Bush's tax cuts… and it sure looks like the idea came to fruition here in Florida.

More than 5 million of Florida's taxpayers had lower income tax bills in 2003 under the President's growth package. More than 1.2 million Florida businesses had the opportunity to use their tax savings to invest in new equipment, hire additional workers, and increase pay to their employees.

The tax cuts worked nationally as well. Economic indicators are positive, across the board.

Homeownership is up, unemployment rates are heading down, and GDP growth has been extremely strong.

This administration came to office when those indicators were not nearly as positive.

The President inherited an economy that was in decline… one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

The President and his administration took these challenges seriously and we have made serious progress in changing the economic direction of this country.

As you've seen here in Florida, the President's tax cuts have worked. They provided the stimulus that was necessary to turn the economic ship around… and they are now encouraging and allowing for the economic growth that is continuing

into the future.

• Economic growth in the second half of 2003 was the fastest since 1984;
• New home construction was the highest in almost 20 years;
• Homeownership levels are at historic highs;
• Manufacturing activity is increasing;
• Inflation and interest rates are low;
• Over a quarter million jobs were created in the last five months of 2003;
• Unemployment claims – both initial claims and continuing claims – are falling, indicating improvement in the labor market;
• And last Monday, the Dow closed at a 31-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: We are on a path to sustained economic growth.

However, there is more to do. We are not, by any means, satisfied.

There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

We can encourage the creation of jobs by sticking to the President's six-point plan for growth.

That includes making health care more affordable and costs more predictable by passing Association Health Plan legislation that would allow small businesses to pool together to purchase health coverage for workers at lower rates.

We also need to promote and expand the advantages of using health savings accounts ... how they can give workers more control over their health insurance and costs.

And we've got to reduce frivolous and excessive lawsuits against doctors and hospitals. Baseless lawsuits, driven by lottery-minded attorneys, drive up health insurance costs for workers and businesses.

The need to reduce the lawsuit burden on our economy stretches beyond the area of health care. That's why President Bush has proposed, and the House has approved, measures that would allow more class action and mass tort lawsuits to be moved into Federal court -- so that trial lawyers will have a harder time shopping for a favorable court.

These steps are the second key part of the President's pro-jobs, pro-growth plan.

Ensuring an affordable, reliable energy supply is a third part.

We must enact comprehensive national energy legislation to upgrade the Nation's electrical grid, promote energy efficiency, increase domestic energy production, and provide enhanced conservation efforts, all while protecting the environment.

Again, we need Congressional action: we are asking that Congress pass legislation based on the President's energy plan.

Streamlining regulations and reporting requirements are another critical reform element that benefit small businesses, who represent the majority of new job creation: three out of every four net new jobs come from the small-business sector! So we need to give them a break wherever we can so they're free to do what they do best: create those jobs.

Opening new markets for American products is another necessary step toward job creation. That's why President Bush recently signed into law new free trade agreements with Chile and Singapore that will enable U.S. companies to compete on a level playing field in these markets for the first time -- and he will continue to work to open new markets for American products and services.

Finally, we've got to enable families and businesses to plan for the future with confidence.

That means making the President's tax relief permanent.

Rate reductions, the increase in the child tax credit and the new incentives for small-business investment – these will all expire in a few years. The accelerated rate reductions that took effect in 2003 will expire at the end of this year. Expiration dates are not acceptable – we want permanent relief.

The ability of American families and businesses to make financial decisions with confidence determines the future of our economy. And without permanent relief, incentives upon which they can count, we risk losing the momentum of the recovery and growth that we have experienced in recent months.

The tax relief is the key stimulus for increased capital formation, entrepreneurship and investment that cause true economic growth.

Budgets work better when the economy is growing... because a growing economy means more jobs. That means more tax revenue... which leads to all-important deficit reduction.

Again, I want to congratulate the hard-working families and businesses of Florida on great economic progress. With the help of your members of Congress, we hope to continue to bring relief from Washington, DC, so you can continue to do what you do best: work hard, grow the economy and create jobs.

Thank you.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 11, 2004
JS-1165

Financial Reconstruction in Iraq"
John B. Taylor
Under Secretary of the Treasury for International Affairs
before the
Senate Banking, Housing, and Urban Affairs Committee
Subcommittee on International Trade and Finance

Introduction

Chairman Hagel, Ranking Member Bayh and other members of the Subcommittee, thank you for inviting me back to testify on the financial reconstruction of Iraq. There have been many significant, positive developments since I last testified in September, and I welcome the opportunity to discuss them with you today.

Just this weekend, during the G-7 finance ministers' meeting in Boca Raton, we had an opportunity to hear from Iraq's Central Bank Governor, Sinan Shabibi, and Finance Minister, Kamel Gailani, about their reform priorities. Both officials participated in a session with the G-7 Ministers, and took the opportunity to underscore their commitment to moving ahead with sound, market-oriented reforms that will underpin private sector-led growth.

They also stressed that their vision of a new Iraqi economy shares the following key principles: 1) openness and transparency of Iraq's institutions; 2) the creation of strong incentives for private sector development; 3) close economic and financial integration with the international community; 4) implementation of international standards and best practices; and 5) a social safety net that addresses the needs of all Iraqis.

These officials are already taking meaningful actions to back up their statements. For example, Iraq's Central Bank Governor recently announced three major actions that will have far- reaching consequences for the development of Iraq's financial sector: 1) the selection of three foreign banks to receive a license to operate in Iraq; 2) a plan to liberalize interest rates by March 1; and 3) passage, soon, of a new Central Bank law.

Today, I would like to tell you more about these developments, as well as update you on the progress that has been made on currency reform, reducing Iraq's international debt burden, and mobilizing international support to meet Iraq's reconstruction needs.

Currency Reform

I would like to begin by highlighting one of the most important accomplishments in the financial sector – the successful introduction of a new currency in Iraq. When I last spoke before this committee, I laid out our strategy for replacing the old national currencies – the Swiss dinar and the Saddam dinar – with a new, unified national currency. I am happy to report that this plan was successfully implemented as scheduled between October 15 and January 15.

Printing and delivering this currency on time was an enormous feat -- the equivalent of twenty-seven 747 plane loads of currency were delivered to Iraq and distributed to the public through approximately 240 exchange sites, mostly bank branches, under a significant security threat.

By all accounts, the Iraqis have wholeheartedly embraced their new dinars. Not

only are the new notes much more difficult to counterfeit -- a chronic problem under the old currency regime -- the Iraqis now have six denominations available, up from only two. And the value of the currency has steadily increased since its introduction. Now the challenge is to manage this new currency in such a way as to provide a stable monetary foundation for a healthy financial system and vigorous reconstruction.

Restoring and Revitalizing the Banking Sector

Another area where meaningful progress has been made is in the banking sector. In my last testimony, I reported that Treasury advisors were assessing the conditions of Iraqi's state-owned and private banks. Since then, we have learned that Rasheed and Rafidain banks – the two large state-owned banks which controlled over 85% of banking assets -- are at best marginally capitalized, and have loan portfolios with a high concentration of non-performing loans. Compounding these problems is the lack of comprehensive, modern accounting standards and systems. We also discovered that although these two banks have an extensive network of more than 360 branches throughout the country, each branch has operated largely as an independent unit. As a result, Iraq lacks centralized management and an integrated system for making and clearing payments.

An evaluation of the private banks uncovered significant problems as well. It turns out the 17 private banks in Iraq served predominantly to take deposits rather than finance investments, and that the largest of these private banks had only $1 million in capital.

Finally, our evaluation of Iraq's legal regime showed that Iraq lacked a competent supervisory or effective regulatory structure to oversee the financial sector.

Despite this bleak assessment, the Iraqi bankers we engaged with from the private and public sectors – as well as key finance officials – shared an eagerness to adopt the reforms necessary to develop a modern, efficient financial sector. Though they lack technology, resources and experience, after only a few months, significant progress has already been made toward this goal.

First, the Iraqis are moving towards the establishment of a modern legal and regulatory framework for the financial sector. For example, working with experts from central banks and other governments and the International Monetary Fund, we helped Iraq to prepare a modern Banking Law and a new Central Bank Law, both based on international best practices. The Banking Law was enacted in late September and contains many provisions designed to support the development of a strong, robust banking sector, including higher minimum capital requirements (10 billion dinars, or more than $6 million), and more rigorous standards for bank licensing and for bank governance.

We expect the Central Bank Law to be adopted soon by the Iraqi Governing Council. It will not only confirm the independence of the Central Bank established by a July 7 CPA order, but will also prevent the Central Bank from engaging in inflationary financing of the government. Indeed, it establishes price stability as the primary macroeconomic objective of monetary policy.

Second, the Central Bank Governor announced that interest rates on all domestic financial instruments – loans, deposits and securities – will be fully liberalized by March 1. This measure is an important step in the direction of creating a modern, efficient financial sector, because it will enable lenders and borrowers to make their own decisions rather than having them determined by fiat and top-down directives issued by the Central Bank.

And third, the Iraqis have taken significant steps to reinvigorate private banks in Iraq. Under Saddam's regime, private banks fared poorly – they controlled less than 8% of total banking assets, used antiquated technology, and offered very limited services. Despite their weaknesses, Iraq's private bank mangers have been eager to develop their capacity to operate as modern, commercial bankers. As provided under the new Banking Law, these banks can now provide new services to their clients. Already, ten banks are receiving international payments and remittances, and issuing letters of credit. With 143 functioning branches, international payments and remittances are now estimated at more than $5 million

per day into Iraq. This influx of funds will play a major role in financing investment and consumption.

While some of the existing private banks are expected to develop into fully functioning financial institutions, Iraqi authorities decided that it would be important for foreign banks to operate in Iraq because of the experience, technology and resources they can offer. The new bank law permits up to six foreign banks to enter the Iraqi market over the next four years. This is in sharp contract to the previous regime, which permitted only Arab banks to enter Iraq's market.

Following a request for applications issued in November, Iraq received fifteen applications for a foreign bank license. On January 31, the Central Bank Governor announced the three finalists for the first set of licenses to be awarded – Hong Kong Shanghai Banking Corporation, the National Bank of Kuwait, and Standard Chartered Bank from the U.K. The Central Bank anticipates that all three will be granted a license by mid-March. Already, the National Bank of Kuwait has announced its intent to purchase 85% of one of the existing private banks.

Next on the agenda is reform of the state-owned banks. Substantial and sustained restructuring of management, organization, personnel and systems is needed to make these banks competitive. The Iraqi authorities are now working with Treasury advisors to develop a strategy for dealing with the state-owned banks so they can operate profitably and provide a wide array of financial services to the Iraqi economy. In the meantime, we are working with the Iraqis to ensure that the state-owned banks can provide basic services, such as taking deposits, clearing checks and making loans to support business activity. For the quarter ending November 30, 2003, Iraq's two large state-owned commercial banks, Rafidain and Rasheed, extended loans totaling about $6 million, primarily to small and medium enterprises.

Trade Bank of Iraq

Given the limited capacity of the Iraqi banking system, we also went forward with a plan to open a Trade Bank in order to facilitate the imports and exports urgently needed to support Iraq's reconstruction and the transition from the UN's oil for food program. When I reported on this initiative last September, the CPA had completed a competitive bidding process for management of the Bank, and negotiations for its establishment were underway. The Bank opened on December 4, 2003, and is now fully operational. To date, the Trade Bank of Iraq has issued over 200 Letters of Credit worth $190 million for most Ministries and several state-owned enterprises.

In addition, sixteen export credit agencies have signed an agreement with the CPA and the Trade Bank under which they will provide guarantees and short-term credit lines valued at $2.4 billion.

Iraq's International Debt

I want to turn now to the issue of Iraq's substantial foreign debt problem. Last September, the G-7 Finance Ministers committed to making their best efforts to resolve this issue by the end of 2004. We have made significant progress towards this goal.

As an indication of the priority we place on this issue, the President asked former Secretary of the Treasury and of State James Baker to serve as his Special Presidential Envoy to work with the world's governments at the highest levels in seeking to restructure Iraq's official debt burden.

Over the past two months, Secretary Baker successfully secured commitments from leaders throughout Western Europe, Asia, and the Gulf States to provide at least substantial debt reduction for Iraq in 2004. Final agreement on the amount and terms of this reduction will be negotiated between Iraq and its creditors, including through the Paris Club.

We are also continuing our efforts to obtain the best possible data on how much debt Iraq owes. Current estimates put Iraq's external debt burden around $120 billion. Paris Club members are owed roughly $40 billion -- $21 billion in principal and roughly an equivalent amount in late interest. Non-Paris Club governments, chiefly the Gulf States, and private creditors hold the rest.

efficient provider of services, a quality employer, and a fair competitor long into the 21st century.

While the Administration may not agree with every aspect of each of the 35 recommendations, we encourage Congressional leaders to carefully consider how the full range of recommendations for legislative consideration might be incorporated in meaningful, comprehensive postal reform.

According to the Commission, 16 of the 35 recommendations do not require any legislative action. The Commission concluded that the Postal Service could implement each of these without any undue delay connected with legislative changes. I also note that the Postal Service's Transformation Plan of April 2002 and the Commission's recommendations are not incongruous; in fact, they are remarkably similar. While I understand that the Postal Service's management is prudent to take time to carefully analyze proposed changes and implement reform actions in a sound manner, I take this opportunity to underscore the Administration's strong support for the Postal Service's efforts to implement reforms as expeditiously as possible. As Postmaster General Potter has frequently stated, the Transformation Plan is a blueprint for positive change and should remain a guideline for future changes. We agree, and would add the Commission's recommendations to this action list.

In outlining the circumstances that led to where we are today, we must add the Civil Service Retirement System (CSRS) Postal Funding Reform Act, signed into law by the President in April 2003. As you well know, this Act contributed significantly to financial recovery of the Postal Service, and is a tribute to the hard work and dedication of the members of this panel in particular. Thanks to this legislation, which allowed a transformation of the Postal Service's CSRS regime into a calculation mechanism that matches the Federal Employee Retirement System (FERS), the Postal Service immediately yielded an estimated $78 billion financial gain. We believe that this has established the appropriate funding provisions for CSRS. Despite this enormous one-time gain, the Postal Service is not yet "out of the woods." Even with the strong leadership of Postmaster General Potter and the Postal Service's Board of Governors to drive an ever more competitive organization, more needs to be done. That is why we are here today.

Last month the Administration announced its support for comprehensive postal reform and articulated five principles to guide congressional debate. The Administration deliberately chose not to be overly prescriptive. We feel strongly that the following five guiding principles can frame a long-term, comprehensive, solution for the challenges that loom on the short and long-term horizon.

Implement best practices The Administration supports comprehensive reform that ensures that the Postal Service's governing body is equipped to meet the responsibilities and objectives of a business of this size and scope. We recognize the hard work of the present and past Board of Governors, as well as postal management and its workforce. However, we believe that it is time to reflect on whether improvements in corporate governance can be incorporated that will add further value for ratepayers, taxpayers, and the Postal Service's workforce and management. As was stated in the President's Commission Report: "The Postal Service should meet the highest standard of corporate leadership...applying the best business practices of the private sector to delivering the nation's mail."

Enhance transparency In keeping with our desire to implement best practices, we seek postal reform legislation that takes steps to ensure that important factual information on the Postal Service's operations and performance is accurately measured and made available to the public. The Postal Service should provide more detailed financial information, including product-by-product financial statements and expanded financial reporting, e.g., voluntary SEC reporting. We also believe there is merit to recognizing the aggregate unfunded post-retirement health liabilities and the annual current cost of such liabilities, either directly on the balance sheet or, at least, in notes to the financial statements. Given the important service this organization provides to the American people, I believe that efforts to facilitate greater access to information can contribute to better decision-making, further enhance trust among stakeholders, and improve oversight.

Provide for greater operating flexibility In return for increased transparency and accountability, and given its self-financing obligation, the Administration believes that the Postal Service's governing body and management should have greater authority to reduce costs, set rates, and adjust key aspects of its business in order to meet its obligations to customers in a dynamic marketplace. In doing so, we urge caution and care to avoid unintended disruption of market forces.

Foster greater accountability Given its existing monopoly, potentially greater flexibility for operations, and its competitive position in some important segments in the delivery marketplace, we urge Congress to enact legislation that ensures that there is appropriate independent oversight to protect consumer welfare and universal mail service. We would like to see reform legislation that provides the corporate governing body with necessary tools to properly motivate postal management to achieve key objectives such as increasing productivity, enhancing service, and improving labor relations. An independent regulatory body must have sufficient authority to fulfill its oversight responsibilities.

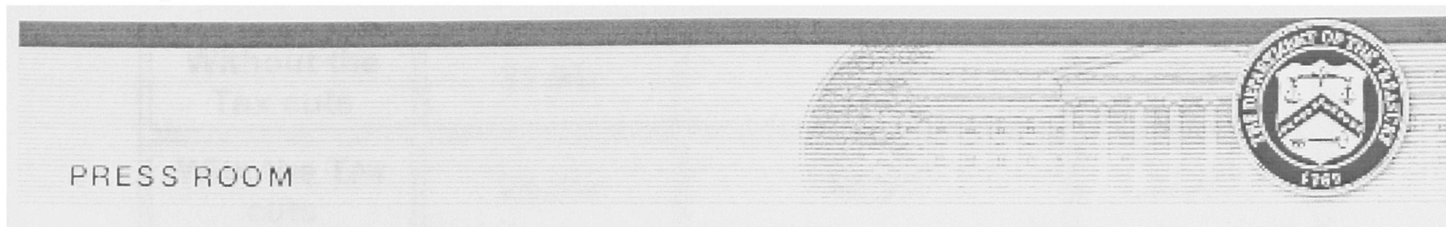
Ensure self-financing The Administration is committed in its desire to see a Postal Service that is financially self-sufficient, covering all of its obligations. We believe that ratepayers should be responsible for covering liabilities, including the off-balance sheet, unfunded liabilities. By so doing, the Postal Service remains motivated to operate in a manner that strengthens the financial and operational health of the Postal Service.

Postal reform is not the only pressing matter involving the Postal Service that is currently before the Congress. The matter of enacting a comprehensive postal reform bill comes at virtually the same time as a related matter currently under consideration by Congress - modification of the CSRS Postal Funding Reform Act. There are two issues under consideration. First, whether Treasury or the Postal Service should be responsible for a share of the costs paid to retired employees of the Postal Service that arise from increasing Civil Service pension benefits because of military service. In this regard, as mentioned earlier, the Administration continues to believe that the Postal Service should remain responsible for these costs and would oppose a modification to the Act. Second, whether the Postal Service should be required to maintain an escrow account that will be disbursed at the discretion of the Congress. The Administration believes that it is optimal for Congress to act expeditiously on both postal reform and the disposition of the escrow as a bundled whole.

The Administration sees postal reform as an integrated whole. It is crucial to address all major aspects of the Postal Service's cost and revenue lines, its balance sheet and off-balance sheet components, its corporate governance, its competitors, as well as the taxpayers and ratepayers. Reform should be characterized by the five principles that, when implemented, will ask each stakeholder to accept shared sacrifice in order to achieve a better, stronger, more accountable and transparent, Postal Service.

Issues surrounding postal reform are, indeed, complex. We are in the presence today of Congressional leaders, such as Congressman McHugh and others, who have spent a tremendous amount of time dedicated to making the Postal Service better. Postmaster General Potter's sustained dedication to achieve this objective must also be recognized. The issues that are involved with postal reform are complex; however, the Administration stands ready to work with you to take this critical issue forward.

Thank you. I will be pleased to answer any questions that you may have.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 12, 2004
JS-1167

Testimony Of Pamela F. Olson
Assistant Secretary (Tax Policy)
United States Department Of The Treasury
Before The Committee On Ways And Means
United States House Of Representatives

Mr. Chairman, Congressman Rangel, and distinguished members of the Committee:

Thank you for the opportunity to appear before you today to discuss the tax proposals included in the President's Fiscal Year 2005 Budget.

Over the last three years, the President and Congress have responded with courage to the recession and to a number of external crises that put additional, extraordinary, strain on that economy. The end of the high-tech bubble and its consequences for the stock market, the revelation of years of wrong-doing on the part of certain corporations and their executives, the impact of the September 11 attacks, and the uncertainties of the war on terror and the conflicts in Afghanistan and Iraq, are all at the root of the recent economic difficulties. These events worsened and prolonged the weaknesses in the economy.

Fiscal policy has played a crucial role in responding to these events. The tax cuts enacted in 2001 were an important factor in making the downturn one of the shallowest on record. Together with an expansionary monetary policy embodied in a series of deep interest rate cuts, the tax cuts provided support to a weakening economy at a critical juncture. The stimulus bill enacted in 2002 provided vital support to the economy in a key area of weakness – corporate investment. The temporary bonus depreciation provision, for example, provided the needed incentive for new corporate investment at just the right time.

While the tax cuts of 2001 were essential to keep the recession from deepening, the 2003 tax cut provided the needed lift to allow the nascent recovery to continue and gain strength. Immediate support to the economy was provided through the acceleration of the lower tax rates, expansion of the child credit, and marriage penalty relief. Weakness in corporate investment was addressed by reducing the double tax on corporate income through the lower tax rate on dividends and capital gains. This change lowered the cost of equity capital and provided an important stimulus to corporate investment. The increase in small business expensing and bonus depreciation provided additional stimulus to corporate investment.

With these vital changes in tax policy, we now have a robust economic recovery with strong economic growth and tightening labor markets that are beginning to put Americans back to work. Moreover, the tax cuts already enacted will continue to spur economic growth. The Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) will put another $146 billion into the economy this year with $100 billion in the first half of the year.

The tax cuts have lowered the marginal effective tax rate on new investment

	Corporate Sector	Non-Corporate Business Sector	Business Sector

Without the Tax cuts	31.9%	20.8%	27.6%
With the Tax cuts	26.3%	18.9%	23.4%
% Change	17.6%	-9.1%	-15.2%

But the tax changes enacted over the past three years have done much more than address and respond to the economic difficulties and crises we have faced. They also laid the ground work for strong economic growth in the future. The lower tax rates improve incentives. After-tax rewards from working are now substantially higher. The taxes paid by entrepreneurs, who tend to pay taxes through the individual income tax, are now lower. The rewards to their innovation and risk taking are greater. The cost of equity capital and investing has been reduced. More risk-taking, investment, and innovation mean higher productivity and greater capital accumulation. A larger capital stock translates into higher living standards for all in the future.

Moreover, the tax changes enacted over the past several years have been fair and balanced. Without the tax cut, the bottom 50 percent of taxpayers would have paid slightly more than 4 percent of individual income taxes. As shown on the chart below, now they pay even less – 3.6 percent. In contrast, the top 5 percent of taxpayers pay a larger share – 52.8 percent of individual income taxes rather than 50.2 percent without the tax cuts. The same is true for the highest income taxpayers – the top 1 percent.

Higher income taxpayers pay a larger share of individual income taxes under the President's tax cuts

	Top 1%	**Top 5%**	**Top 10%**	**Top 25%**	**Top 50%**	**Bottom 50%**
Share of Individual Income Taxes [Share of Adjusted Gross Income]						
With the Tax Cuts	32.3	52.8	64.8	83	96.4	3.6
Without Tax Cuts	30.5	50.2	62.6	81.8	95.9	4.1
Note: Calculations are for 2004. U.S. Treasury, Office of Tax Analysis.						

This group now pays 32.3 percent of all individual income taxes, rather than 30.5 percent before the tax cuts were enacted.

Much remains to be done, however. Making the tax cuts enacted in 2001 and 2003 permanent, promoting savings, making health care more affordable, reducing the barriers to homeownership, simplifying the tax system, ensuring the integrity of the tax system by preventing abusive transactions, and responding to the WTO decision on the extraterritorial income exclusion (ETI) provisions are all important priorities reflected in the President's budget proposals. I will focus on each of these priorities in turn.

Permanence: A Stable, Certain Tax Code

The tax reductions made in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and JGTRRA proved essential for promoting economic growth and will help to ensure higher living standards in the future. If these provisions are allowed to sunset, taxes will increase: for many individuals after 2004, for many small businesses in 2006; for investors beginning in 2009, and again for most taxpayers beginning in 2011.

An uncertain tax code imposes real costs on the economy. Uncertainty makes it difficult for workers and businesses to plan for the future and increases investment risk. The possibility of higher taxes increases the cost of equity capital to businesses and reduces individuals' after-tax rewards to working and investing. A higher cost of equity capital and lower rewards to workers and investors dampen long-run economic growth.

Permanent extension of the tax cuts enacted by the President and the Congress will provide a more certain tax environment for workers and businesses to plan and invest, both reducing complexity and continuing to support a growing economy. The revenue cost of making the tax cuts permanent ($989 billion) is only a small percentage of the revenue of the federal government over the 10-year budget window. Moreover, the cost is only a tiny fraction of the United States economy over this same period.

In addition to uncertainty, failure to make the tax cuts permanent will inflict a real blow to the economy. Allowing the tax cuts to expire amounts to nothing more than a massive tax increase on the vast bulk of individual and business taxpayers.

Towards a Long-Term Solution to the AMT

The expected growth in the individual alternative minimum tax (AMT) is a major problem in the tax code that must be addressed. The AMT was first enacted in the late 1960s to target a small number of very high income taxpayers who paid little or no tax. The stage was set for the AMT's growth when the regular tax was indexed in the early 1980s but the AMT was not. Other changes throughout the 1980s and 1990s compounded the problem.

Now the AMT is a tax that is beginning and will continue to affect increasing millions of taxpayers. It will reach into the ranks of the middle class, potentially denying taxpayers the benefit of many of the deductions, credits and lower tax rates available under the regular tax system. The AMT also significantly increases the complexity of tax filing for taxpayers subject to the AMT and for millions of additional taxpayers who must complete AMT forms only to determine they are not subject to the AMT

The AMT's future growth must be addressed. The President's budget extends through 2005 the temporary increase in the AMT exemption amounts and the provision that allows certain personal credits to offset the AMT. These temporary provisions will keep the number of taxpayers affected by the AMT from rising significantly in the near-term. More importantly, they will allow the Treasury Department the time necessary to develop a comprehensive set of proposals to deal with the AMT in the long-term. Because of the revenues involved and the number of taxpayers affected, any long-term solution to the AMT could well require significant changes to the regular income tax. The Treasury Department looks forward to its task and to working with this Committee to find a long-term solution.

Simpler Savings Options for All

Americans continue to save at a very low rate relative to historical standards and our major trading partners. The President has put forward in this year's Budget a modified version of his savings proposal to help address this low rate of saving. The proposal carefully balances the need for a simpler approach for providing accessible tax-preferred savings options to all Americans and preserving the employer-provided pension system, which has been the foundation for meeting the retirement savings needs for millions.

Saving is made simpler by replacing the existing web of tax-preferred saving options with two new savings vehicles: Retirement Savings Account (RSAs) and Lifetime Savings Accounts (LSAs). These savings vehicles allow everyone to contribute regardless of age or income. The simplicity of these new savings

vehicles will help encourage individuals, especially lower income individuals, to save.

Lower income individuals often do not have the resources to save for the distant future and are unwilling to take the risk of locking up their savings in tightly restricted accounts. In addition, these individuals tend not to have access to the sophisticated advice needed to navigate the complex, and often conflicting, rules that govern the existing savings vehicles. LSAs have been designed to make the decision easy: it is a savings vehicle accessible for all, especially low and moderate income individuals. Any money contributed can be withdrawn at any time without penalty. Treasury believes that these more relaxed rules will encourage individuals to save who might otherwise not do so in targeted savings plans because of restrictions on and penalties for withdrawals. As individuals learn to save, and become comfortable doing so, they will do more of it. The lower $5,000 contribution limit, as compared to the proposal in the FY 2004 Budget, will minimize the effect of these proposals on employer plans.

The proposal for RSAs would simplify the range of choices for taxpayers saving for retirement. The proposal takes the easy to understand Roth IRA and makes it available to all. Any taxpayer can contribute up to the lesser of $5,000 or their earned income. Unlike current law, however, withdrawals could only be made for retirement, beginning at age 58. RSAs are the perfect complement to LSAs: targeted, tax-favored savings coupled with savings for any reason.

The proposal for Employer Retirement Savings Accounts (ERSAs) would consolidate six different types of employer contributory plans into a universal account. The proposal has been modified from the previous FY 2004 Budget proposal to enhance flexibility and encourage small businesses (10 or fewer employees) to fund an ERSA by contributing to a custodial account, which is similar to a current-law IRA.

A third proposal would credit Individual Development Accounts (IDAs) to encourage and assist lower-income individuals save. This proposal would provide dollar-for-dollar matching contributions of up to $500 targeted to lower income individuals. Matching contributions would be supported by a 100 percent credit to sponsoring financial institutions.

Together, these proposals further promote an ownership society by removing barriers to savings, reducing complexity, and improving fairness by providing the benefits of tax preferred savings to everyone, regardless of financial sophistication or capacity to save for the very long-term.

Reducing Barriers to Homeownership

A significant barrier to homeownership continues to be the supply of affordable housing for lower income individuals. To address that need, the President has proposed a $2.4 billion ($16 billion over 10 years), 5-year Single-Family Affordable Housing Tax Credit of up to 50 percent of the project costs of rehabilitation and construction of affordable homes, provided they are offered to homebuyers with incomes of not more than 80 percent of area median income. The tax credit would eventually result in an additional 200,000 affordable single-family homes becoming available through construction or rehabilitation.

Affordable Health Care is a Priority

Expanding access to health insurance remains an important goal of the President and is reflected by his continued commitment in this area. The lack of access to affordable health insurance is a complex problem that requires a comprehensive approach focusing on different segments of the uninsured with policies tailored to meet their needs. There is no one size fits all solution; a policy that excels in one dimension may do poorly in others. The high and rising cost of health insurance is a key factor that limits access. Policies that help control costs will make insurance more affordable through lower premiums.

Health Savings Accounts (HSAs), enacted as part of the recently-passed Medicare Reform legislation, are a significant step towards promoting cost consciousness through greater reliance on individual choice and high deductible plans. HSAs, now part of current law, are complemented by a new proposal in the President's Budget

for an above-the-line deduction for premiums to purchase the high deductible health plans (HDHP) necessary in order to have an HSA. The proposal generally helps level the playing field for a segment of the population that does not have employer-sponsored coverage.

The proposal for a refundable, advanceable health insurance tax credit would help make insurance more affordable for lower income individuals. The credit amount under the proposal would vary with family size, mirroring the relationship of actual health insurance premiums. The credit is targeted to low-income individuals and families, who are the least likely to have employer-based health insurance, resulting in the efficient use of the subsidy. Together, these policies promote affordability and access, and help encourage greater cost consciousness by giving individuals a greater stake in their health care choices.

Protecting Defined Benefit Plans and Promoting Fair Treatment for Older Workers in Conversions to Cash Balance Plans

The President's budget reflects the importance of preserving defined benefit pension plans and the benefits they provide to workers and their families. In addition to the proposal to fix the flawed interest rate used to determine the amount of contributions a plan sponsor must make to its defined benefit plan, the budget contains three interrelated proposals that recognize the importance of cash balance plans in providing retirement security to millions of Americans. The first proposal would ensure that companies converting from a traditional defined benefit plan to a cash balance pension include a fair transition for older workers. A five-year hold harmless provision would be required in a cash balance conversion, so that workers would continue to earn benefits under the greater of the prior plan formula or the cash balance formula for five years after the conversion. The second proposal would clarify that cash balance plans do not violate the age-discrimination rules that apply to pension plans as long as they treat older workers at least as well as younger workers. This would remove uncertainty created by inconsistent federal court decisions and would ensure the future of cash balance plans. The final proposal would eliminate the "whipsaw" effect, which acts as an effective cap on the interest credits that cash balance plans can provide to workers. This would permit companies to give higher interest credits, allowing larger retirement accumulations for workers.

Simplification of an Overly Complex Tax Code

In a sophisticated economy, a tax code with complex provisions may be unavoidable. It is the price we pay to ensure fairness, to limit government interference with personal and business decisions, and to prevent abuse. On the other hand, unnecessary complexity imposes tremendous burdens on honest taxpayers simply doing their best to comply with the law. The present tax system imposes compliance costs on taxpayers estimated to range from $70 billion to $100 billion per year from the individual income tax alone. Compliance costs also are onerous for business taxpayers, especially small businesses, while the typical Fortune 500 company spends almost $4 million a year on tax matters.

For these reasons, it is crucial that we continue efforts to simplify the tax laws. The 2005 Budget includes several new simplification proposals. All of these proposals address complexities borne by individuals and families. They do not represent an exhaustive list; instead, they serve as examples of the many steps that can and should be taken to make the tax code easier to understand and comply with. The Treasury Department looks forward to working with this Committee to identify other areas where significant improvements can and should be made.

Stopping Abusive Transactions

Voluntary compliance with the tax laws is undermined when taxpayers use abusive transactions to avoid paying the taxes they rightfully owe. For the past three years, the Administration has acted aggressively to restore confidence in the tax system by halting the promotion of abusive transactions and bringing taxpayers back into compliance with the tax laws. The President's Budget builds on these efforts and information gathered through IRS compliance programs. The new legislative proposals close loopholes and target identified abusive transactions and practices. As other abusive transactions are identified, the IRS will challenge the transactions in audits, and the Treasury Department and the IRS will work with Congress to enact any legislation necessary to address such transactions.

One proposal deserves particular mention. The Administration has proposed to limit certain types of abusive leasing transactions, known as SILOs.

These arrangements are entered into with tax-indifferent parties, such as foreign governments, domestic municipalities, and tax-exempt organizations. They purport to be leasing transactions but, in substance, provide no financing to the tax-indifferent party aside from a fee. These arrangements have no meaningful financial or economic utility other than the transfer of tax benefits to a U.S. taxpayer (by means of a purported "sale" of property) in exchange for the payment of an accommodation fee to the tax-indifferent party.

Although Treasury has been aware of SILOS for some time, the extent of the problem has only recently come to light. Our data indicates that as much as $750 billion dollars of SILOs have been done in just the last four years. We have every reason to believe that, left unchecked, this trend will continue and grow. Because these transactions essentially involve no risk to either party, and require very little in the way of actual cash investment, corporations seeking to reduce their U.S. tax liability will face no economic bar to seeking out these arrangements on an increasing basis.

SILOs represent a threat to the viability of the corporate tax base. They present a ready-made tool for self-help tax relief for large corporations and consortiums of smaller ones. Indeed, the magnitude of SILO transactions is such that the Treasury Department had to re-estimate and reduce its baseline estimate of corporate tax receipts over the ten-year budget window. It is essential that Congress deal with this issue. Otherwise, any corporation with the wherewithal to do so could plan itself out of the corporate income tax. The American citizenry rightfully expect their government to ensure that all taxpayers pay the taxes they owe, unreduced by artificial transactions. Congress should act promptly to ensure that SILOs are not permitted to continue.

At the same time, in addressing the SILO problem, it is not our goal to interfere with garden variety leasing transactions that have been entered into for many years and that involve legitimate financing or refinancing of assets. The detailed SILO proposal in the President's budget permits legitimate lease transactions to continue. We look forward to working with this Committee to ensure that legislation is enacted that leaves legitimate transactions unscathed while preventing abusive lease transactions from going forward.

Responding to WTO Decisions on ETI Provisions

The Extraterritorial Income ("ETI") provisions of our tax law, like the prior-law foreign sales corporation provisions, have been found to be inconsistent with World Trade Organization (WTO) rules. The WTO has authorized the imposition of trade sanctions against U.S. exports up to the level of $4 billion per year, and the European Union has adopted a plan providing for sanctions to be phased in beginning next month if the ETI provisions remain in the law.

Honoring our WTO obligations requires repeal of the ETI provisions. At the same time, meaningful changes to our tax law are required to preserve and enhance the competitiveness of U.S. businesses operating in the global marketplace. Thus, the necessary repeal of the ETI provisions should be coupled with other tax changes that promote the competitiveness of American manufacturers and other job-creating sectors of the U.S. economy. Tax law changes that would provide a benefit to these vital contributors to the U.S. economy include across-the-board corporate tax rate reduction, expansion and permanence of the research credit, improvements in depreciation rules, extension of NOL carryback rules, AMT reform, business tax simplification, and rationalization of the international tax rules. The Administration intends to continue to work with this Committee and the Congress on prompt enactment of legislation that brings our tax law into compliance with WTO rules and makes changes to the tax law to enhance the global competitiveness of American businesses and the workers they employ.

Conclusion

Thank you again, Mr. Chairman and members of the Committee, for the opportunity to appear before you today. We look forward to working together with this Committee and others in the Congress to promote tax policies that continue to

provide a sound foundation for economic growth.

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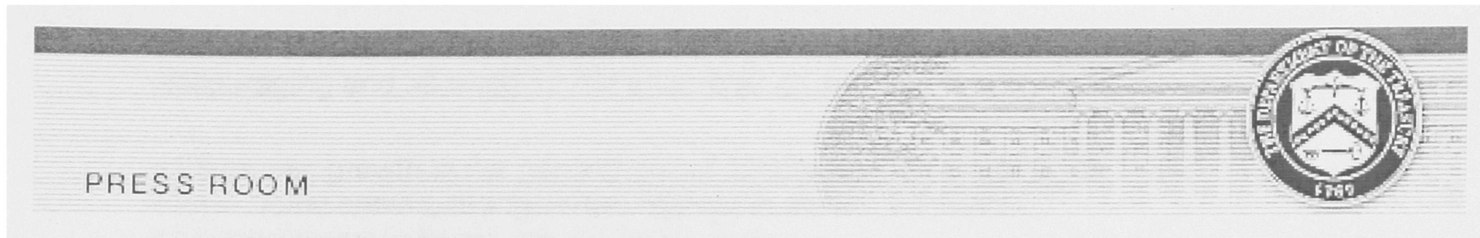

FROM THE OFFICE OF PUBLIC AFFAIRS

February 12, 2004
JS-1168

Secretary John W. Snow
Opening Statement before the Senate Finance Committee
Testimony on Revenue Proposals in the President's FY 2005 Budget
Thursday, February 12, 2004

Thank you, Mr. Chairman.

Thank you all for having me here today to talk about the President's budget.

I believe you'll find that this budget reflects the priorities of our nation as well as the leadership of President George W. Bush.

The over-riding theme of the budget, and the President's plan for the future, is that a safer world is a more prosperous world. That's why I'll be discussing both national and economic security here today.

Decisions about how to collect and spend taxpayer dollars – for this is what a budget is – must be made with both caution and vision.

The Fiscal Year 2005 budget proposal is, therefore, a plan that does three core things:

• One: Keeps Americans safe by providing the resources necessary to win the war on terror and protect our homeland;
• Two: Increases the economic security of our citizens as well, by strengthening our economy; and
• Three: Exercises the kind of spending discipline that is required by a government that respects the source of its money (hard-working taxpayers!) and is unwilling to live with a deficit.

Discussions of our budget and our economy are not, and should not, be separate. The two are inextricably connected.

Today, our economy is doing better.

Homeownership is up, unemployment is heading down, and GDP growth has been strong.

This administration came to office when those indicators were not nearly as positive.

The President inherited an economy that was in decline… one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

The President and his administration took these challenges seriously and we have made serious progress in changing the economic direction of this country.

The President's tax cuts – passed by you – have worked. They provided the

stimulus that was necessary to turn the economic ship around... and they are now encouraging and allowing for the economic growth that is continuing into the future.

• Economic growth in the second half of 2003 was the fastest since 1984;
• New home construction was the highest in almost 20 years;
• Homeownership levels are at historic highs;
• Manufacturing activity is increasing;
• Inflation and interest rates are low;
• Over 360,000 jobs have been created in the past five months;
• Unemployment claims – both initial claims and continuing claims – are well off their peaks last year, indicating improvement in the labor market;
• This Wednesday, the Dow closed at a 32-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: economic growth is robust and will be sustained.

However, there is more to do. We are not, by any means, satisfied.

There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

Our budget addresses that need by continuing to focus on improving our economy.

For example, the President's Jobs for the 21st Century plan, announced in his State of the Union Address, directs the resources of several branches of government toward matching skills with jobs, and helping workers acquire the skills they need to qualify for the jobs in their community.

We can also encourage the creation of jobs by sticking to the President's six-point plan for growth.

That includes making health care more affordable and costs more predictable.

We can do this by passing Association Health Plan legislation that would allow small businesses to pool together to purchase health coverage for workers at lower rates.

We also need to promote and expand the advantages of using health savings accounts ... how they can give workers more control over their health insurance and costs.

And we've got to reduce frivolous and excessive lawsuits against doctors and hospitals. Baseless lawsuits, driven by lottery-minded attorneys, drive up health insurance costs for workers and businesses.

The need to reduce the lawsuit burden on our economy stretches beyond the area of health care. That's why President Bush has proposed, and the House has approved, measures that would allow more class action and mass tort lawsuits to be moved into Federal court -- so that trial lawyers will have a harder time shopping for a favorable court.

These steps are the second key part of the President's pro-jobs, pro-growth plan.

Ensuring an affordable, reliable energy supply is a third part.

We must enact comprehensive national energy legislation to upgrade the Nation's electrical grid, promote energy efficiency, increase domestic energy production, and provide enhanced conservation efforts, all while protecting the environment.

Again, we need Congressional action: we ask that you pass legislation based on the President's energy plan.

Streamlining regulations and reporting requirements are another critical reform element that benefit small businesses, who represent the majority of new job creation: three out of every four net new jobs come from the small-business sector! Let's give them a break wherever we can so they're free to do what they do best: create those jobs.

Opening new markets for American products is another necessary step toward job creation. That's why President Bush recently signed into law new free trade agreements with Chile and Singapore that will enable U.S. companies to compete on a level playing field in these markets for the first time -- and he will continue to work to open new markets for American products and services.

Finally, we've got to enable families and businesses to plan for the future with confidence.

That means making the President's tax relief permanent.

Rate reductions, the increase in the child tax credit and the new incentives for small-business investment – these will all expire in a few years. The accelerated rate reductions that took effect in 2003 will expire at the end of this year. Expiration dates are not acceptable – we want permanent relief.

The ability of American families and businesses to make financial decisions with confidence determines the future of our economy. And without permanent relief, incentives upon which they can count, we risk losing the momentum of the recovery and growth that we have experienced in recent months.

The tax relief is the key stimulus for increased capital formation, entrepreneurship and investment that cause true economic growth.

Budgets work better when the economy is growing… because a growing economy means more jobs. That means more tax revenue… which leads to all-important deficit reduction.

Which leads me to my next area of discussion.

Let me be clear on this:
• The budget deficit that we face today is unwelcome.
• It needs to be addressed.
• The President's budget calls for cutting the deficit in half over the next five years.
• While addressing the deficit, we must remember that it is not historically overwhelming.
• It is understandable, given the extraordinary circumstances of recent history. Remember that we are fighting a type of war that we have never fought before. We are fighting an enemy that requires a much broader variety of government resources than anything we've ever confronted. And we began this fight when we were economically wounded.

What's most important to remember is that we will be able to fight this war and climb out of the deficit.

We can manage this deficit, and we can cut it in half over the next five years by controlling spending and growing our economy.

Three-quarters of the discretionary spending increases during this Administration have been related to the global war on terror and the response to 9/11.

Meanwhile, President Bush has reduced the rate of increase in non-security-related discretionary spending every year he has been in office: to six percent in 2002, five

percent in 2003, and to four percent in the current fiscal year.

For Fiscal Year 2005 we're going to reduce the rate of increase in non-security discretionary spending to less than one percent.

Total annual appropriated discretionary spending will increase by less than four percent next year.

Holding the line on spending – while ensuring that our country is safe and our most important needs, from jobs to health care, are met – will achieve deficit reduction when coupled with all-important economic growth.

Again, this is why the budget cannot be discussed separately from the economy. Separating the two is what gets government into trouble.

Make no mistake; President Bush is serious about the deficit.

We see it as unwelcome, but manageable… and we intend to achieve: rapid deficit reduction.

A recent CBO report raised concerns about this matter, and it is important to note that recent and short-term projected budget deficits and the existence of long-term deficits for Social Security and Medicare are not connected.

These unfunded long-term net obligations are also a concern, and ones that this Administration has highlighted and invited bipartisan dialogue on.

The President has been clear on this: younger workers should have the opportunity to build a nest egg by saving part of their Social Security taxes in personal retirement accounts. His vision for the program is economically wise, and it is that we should make the Social Security system a source of ownership for the American people.

Are we dedicating ourselves to increased spending on the war on terror and protecting the homeland? The answer is yes. Yes, without sacrificing other necessities.

And that is because a nation must be safe in order for it to be prosperous.

A nation of entrepreneurs must also be able to plan, and to be relieved of as many burdens as possible, in order to be prosperous.

All of the budget issues and policy proposals that I've discussed today may seem, at times, to be a complicated recipe. But these ingredients combine to make something that is simply put, and is of utmost importance – and that is economic growth.

Growth is the key to every economic problem we confront. That's why we urge other countries to institute pro-growth policies. It's good for them, and it's good for the global economy that we are a significant part of.
Thank you for hearing my testimony today. I'll be happy to take your questions now.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 12, 2004
JS-1169

Treasury and IRS make it easier for States to use the Health Coverage Tax Credit

Today, the Treasury Department and the IRS issued guidance to make it easier for state governments to elect qualified health insurance that will be eligible for the Health Coverage Tax Credit.

The Health Coverage Tax Credit, which President Bush signed into law as part of the Trade Act of 2002, provides valuable assistance for many Americans who are participating under the Trade Adjustment Assistance program or who are receiving benefits under a pension plan that has been assumed by the Pension Benefit Guaranty Corporation. This assistance consists of an advanceable, refundable tax credit equal to 65% of the cost of qualified health insurance. The principal types of qualified health insurance are private health plans elected by states. This guidance issued today formalizes and clarifies guidance that has been provided to each of the states' governors.

Treasury and the IRS have been working with all the states to get a qualifying program in place for all eligible individuals. So far, 27 states and the District of Columbia have elected plans for all their residents who are eligible individuals. "We want to ensure that everyone eligible for the Health Coverage Tax Credit can have the opportunity to sign up for it. We are concerned about people in the remaining 23 states who are eligible for the credit but cannot use it," said Roy Ramthun, senior advisor for health initiatives to the Secretary of the Treasury. "We are working closely with numerous government officials and health plans in these states to encourage them to make this valuable Health Coverage Tax Credit available to their eligible residents. We believe this guidance will make the election process easier."

Related Documents:

- The text of the Revenue Procedure.
- List of states with qualifying health programs.

Part III

Administrative, Procedural, and Miscellaneous

Section 35: Health Insurance Costs of Eligible Individuals

Rev. Proc. 2004-12

SECTION 1. PURPOSE

This revenue procedure provides guidance on how a state elects a health program to be qualified health insurance for purposes of the health coverage tax credit (HCTC) under section 35 of the Internal Revenue Code.

SECTION 2. BACKGROUND

.01 On August 6, 2002, President Bush signed into law the Trade Act of 2002 ("the Act"), Pub. L. 107-210, 116 Stat. 933 (2002). Title II of the Act contains provisions that make assistance available to certain individuals participating in the Trade Adjustment Assistance program (TAA) or receiving payments from the Pension Benefit Guaranty Corporation (PBGC), to enable them to purchase health insurance. The primary mechanism for such assistance is a federal tax credit that is equal to 65 percent of the amount paid by the eligible individual for coverage for the individual and qualifying family members under qualified health insurance. The health coverage tax credit became available on December 1, 2002 and is claimed on the eligible individual's income tax return. Beginning August 1, 2003, the HCTC is also available on a monthly basis as the premium is paid. Under the advance HCTC program, the government's share -- 65 percent of the premium amount paid by the individual -- is combined with the eligible individual's payment of the other 35 percent and paid on a monthly basis, in general to the qualified health plan in which the individual has enrolled.

.02 There are two basic categories of individuals who may be eligible for the HCTC:

(1) TAA recipients (as described in section 2.03 of this revenue procedure), and

(2) PBGC pension recipients who have attained age 55 but who do not have Medicare coverage (as described in section 2.04 of this revenue procedure).

.03 A TAA recipient is any individual who is receiving a trade readjustment allowance under the Trade Act of 1974 for any day of a month, or any individual who would be eligible for such an allowance except that the individual has not exhausted the individual's regular unemployment insurance benefits. In addition, for purposes of this revenue procedure, any individual receiving benefits under the alternative trade adjustment assistance program, established under § 246 of the Trade Act of 1974, 19 U.S.C. §§ 2271-2275 (2003), is also a TAA recipient. All TAA recipients remain eligible for the HCTC (and thus are still considered TAA recipients) for one month after the end of the month that their eligibility for TAA ceases.

.04 A PBGC pension recipient is a person who is receiving a benefit payment from the

PBGC for a month and who has attained age 55 (but who is not entitled to Medicare) on the first day of the month.

.05 There are ten categories of health insurance that may be qualified coverage for purposes of the HCTC:

(1) COBRA coverage: Coverage under a COBRA continuation provision (under § 4980B of the Code; part 6 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1161-1168 (2003); or title XXII of the Public Health Service Act, 42 U.S.C. §§ 300bb-1-300bb-8 (2003));

(2) State-based continuation coverage: Coverage under a state law that requires continuation coverage;

(3) High risk pool: Coverage offered through a qualified state high risk pool (as defined in section 2744(c)(2) of the Public Health Service Act , 42 U.S.C. § 300gg-44(c)(2) (2003));

(4) State employees' health plan: Coverage under a health insurance program offered for state employees;

(5) Comparable state employees' health plan: Coverage under a state-based health insurance program that is comparable to the health insurance program offered for state employees;

(6) State arrangement: An arrangement to offer coverage to HCTC eligible individuals entered into by a state with --

(a) an issuer of health insurance coverage;
(b) an administrator;
(c) an employer; or
(d) a group health plan (including a multiemployer plan);

(7) Private purchasing pool: Coverage offered through a state arrangement with a private sector health care coverage purchasing pool;

(8) Other state plans: Coverage under a state-operated health plan that does not receive any federal financial assistance;

(9) Spousal coverage: Coverage under a group health plan that is available through the employment of the HCTC eligible individual's spouse (but only if the spouse's employer contributes less than 50 percent of the total cost of coverage for the spouse, the eligible individual, and any dependents); and

(10) Individual health insurance: Coverage under individual health insurance if the HCTC eligible individual was covered under the insurance during the entire 30-day period that ended on the date that the individual became separated from the employment that qualifies

the individual as a TAA or PBGC recipient.

.06 Coverage described in paragraphs (1), (9), and (10) of section 2.05 of this revenue procedure -- COBRA coverage, spousal coverage, and individual health insurance -- satisfies the requirements for "qualified health insurance" for all HCTC eligible individuals without any action required by any state.

.07 Coverage described in paragraphs (2) through (8) of section 2.05 of this revenue procedure (state-based continuation coverage or other state-based plans) satisfies the requirements for qualified health insurance only if the state elects to have such coverage treated as qualified health insurance and the coverage satisfies the following requirements:

(1) Qualifying individuals (as defined in section 2.08 of this revenue procedure) must be guaranteed enrollment regardless of their medical status and must be permitted to remain enrolled so long as they pay the premium;

(2) No preexisting condition restriction may be imposed on qualifying individuals;

(3) The premium charged for a qualifying individual may not be greater than the premium for a similarly situated individual who is not a qualifying individual; and

(4) Benefits for qualifying individuals are the same as (or substantially similar to) the benefits provided to similarly situated individuals who are not qualifying individuals.

.08 "Qualifying individuals" are HCTC eligible individuals who have at least 3 months of "creditable coverage" (within the meaning of § 9801 of the Code) prior to seeking enrollment in coverage described in paragraphs (2) through (8) of section 2.05 of this revenue procedure.

SECTION 3. PROCEDURE FOR ELECTING TREATMENT AS QUALIFIED HEALTH INSURANCE

.01 This section sets forth the procedures that a state must follow in order to elect to have coverage described in paragraphs (2) through (8) of section 2.05 of this revenue procedure (state-based continuation coverage or coverage under other state-based plans) treated as qualified health insurance. As described in section 2.07 of this revenue procedure, such coverage is not qualified health insurance unless such an election is made.

.02 To make an election, a state must provide a letter that contains the following information:

(1) Identifies and is signed by the governor or other state official responsible for implementing this decision, including address and telephone number;

(2) Specifies the category or categories of health coverage chosen by the state (from among the categories described in paragraphs (2) through (8) of section 2.05 of this

revenue procedure (state-based continuation coverage or other state-based plans));

(3) Provides the name and policy form number or other unique identifier for each qualifying plan in each category, and provides a name and contact number for the plan administrator or insurance carrier official who can provide additional information, if necessary. This information is required only for coverage described in paragraphs (3) through (8) of section 2.05 of this revenue procedure; it need not be provided for state-based continuation coverage described in paragraph (2) of section 2.05 of this revenue procedure; and

(4) Certifies that the four requirements described in section 2.07 of this revenue procedure are met for each plan being elected under each category.

.03 The letter must be sent to:

Director, Health Coverage Tax Credit
Internal Revenue Service
1111 Constitution Ave, N.W.
W:HCTC/CNN 750
Washington, D.C. 20224

SECTION 4. EFFECTIVE DATE

This revenue procedure is effective March 1, 2004. Elections made before the effective date of this revenue procedure continue to be effective, including those sent to a different address; they do not need to be renewed.

SECTION 5. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1875.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collection of information in this revenue procedure is in section 3. This information will be used to determine if a state health plan is qualified health insurance for purposes of the HCTC. This information collection is voluntary. If a state makes an election, eligible residents of the state may be able to more easily find qualified health insurance for which they can claim the HCTC.

The likely respondents are states. The estimated total annual reporting burden is 26

hours. The estimated annual burden per respondent varies from 1/4 hour to 1 hour, depending on individual circumstances, with an estimated average of ½ hour. The estimated total number of respondents is 51. The estimated frequency of responses is one-time.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

DRAFTING INFORMATION

The principal author of this revenue procedure is Shoshanna Tanner of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this revenue procedure contact Mr. Stephen Finan on (202) 622-1446 or Ms. Tanner on (202) 622-6080 (not toll-free numbers).

State	State Qualified Plans (28 States with Qualified Plans)	
	High Risk Pool	Private Plans
Alabama	X	
Alaska	X	
Arkansas	X	
Colorado	X	
Connecticut	X	X
District of Columbia		X
Florida		X
Illinois	X	
Indiana		X
Iowa	X	
Maine		X
Maryland	X	
Michigan		X
Minnesota	X	
Montana	X	
New Hampshire	X	
New York		X
North Carolina		X
North Dakota	X	
Ohio		X
Pennsylvania		X
Rhode Island		X
South Carolina	X	
Tennessee		X
Texas	X	X
Vermont		X
Virginia		X
West Virginia		X
Total: 28	14	16

FROM THE OFFICE OF PUBLIC AFFAIRS

February 12, 2004
JS-1170

TREASURY CLARIFIES BOSNIAN DESIGNATION
Clarification to Treasury News Release, "Operation Balkan Vice III: Designation of Thirteen Individuals Obstructing the Dayton Peace Accords in Bosnia," February 9, 2004

Three of the thirteen persons designated by Treasury's Office of Foreign Assets Control pursuant to Executive Order 13219, Avdyl Jakupi, Xhezair Shaqiri, and Menduh Thaci were designated for extremist activities, including obstructing, or otherwise acting to undermine the Ohrid Framework Agreement of 2001 and peace and stability in Macedonia, or for acting or purporting to act for or on behalf of any person designated pursuant to the order.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 12, 2004
2004-3-1-13-8-9-22196

U.S. International Reserve Position

'he Treasury Department today released U.S. reserve assets data for the latest week. As indicated in this table, U.S. reserve assets ɔtaled $86,014 million as of the end of that week, compared to $85,368 million as of the end of the prior week.

I. Official U.S. Reserve Assets *(in US millions)*

	January 30, 2003			February 6, 2004		
TOTAL		85,368			86,014	
. Foreign Currency Reserves [1]	Euro	Yen	TOTAL	Euro	Yen	TOTAL
Securities	8,386	14,862	23,248	8,570	14,900	23,469
f which, issuer headquartered in the U.S.			0			0
Total deposits with:						
: Other central banks and BIS	13,606	2,986	16,592	13,876	2,993	16,869
i. Banks headquartered in the U.S.			0			0
i. Of which, banks located abroad			0			0
'i. Banks headquartered outside the U.S.			0			0
i. Of which, banks located in the U.S.			0			0
MF Reserve Position [2]			21,887			21,981
pecial Drawing Rights (SDRs) [2]			12,598			12,652
·old Stock [3]			11,043			11,043
ther Reserve Assets			0			0

II. Predetermined Short-Term Drains on Foreign Currency Assets

	January 30, 2003			February 6, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
·ign currency loans and securities			0			0
·egate short and long positions in forwards and futures in foreign currencies vis-à-vis the U.S. dollar:						

	Euro	Yen	TOTAL	Euro	Yen	TOTAL
2.a. Short positions			0			0
2.b. Long positions			0			0
3. Other			0			0

III. Contingent Short-Term Net Drains on Foreign Currency Assets

	January 30, 2003			February 6, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
1. Contingent liabilities in foreign currency			0			0
1.a. Collateral guarantees on debt due within 1 year						
l.b. Other contingent liabilities						
?. Foreign currency securities with embedded ›ptions			0			0
. Undrawn, unconditional credit lines			0			0
.a. With other central banks						
b. With banks and other financial institutions						
eadquartered in the U.S.						
c. With banks and other financial institutions						
ɜadquartered outside the U.S.						
Aggregate short and long positions of tions in foreign						
rrencies vis-à-vis the U.S. dollar			0			0
. Short positions						
1. Bought puts						
2. Written calls						
Long positions						
1. Bought calls						
?. Written puts						

Notes:

des holdings of the Treasury's Exchange Stabilization Fund (ESF) and the Federal Reserve's System Open Market Account), valued at current market exchange rates. Foreign currency holdings listed as securities reflect marked-to-market values, and s reflect carrying values. Foreign Currency Reserves for the latest week may be subject to revision. Foreign Currency

Reserves for the prior week are final.

2/ The items, "2. IMF Reserve Position" and "3. Special Drawing Rights (SDRs)," are based on data provided by the IMF and are valued in dollar terms at the official SDR/dollar exchange rate for the reporting date. The entries for the latest week reflect any necessary adjustments, including revaluation, by the U.S. Treasury to IMF data for the prior month end.

3/ Gold stock is valued monthly at $42.2222 per fine troy ounce.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 13, 2004
JS-1171

Secretary John W. Snow
Opening Statement before the Senate Committee on the Budget
Testimony on Revenue Proposals in the President's FY 2005 Budget
Friday, February 13, 2004

Thank you, Mr. Chairman.

Thank you all for having me here today to talk about the President's budget.

I believe you'll find that this budget reflects the priorities of our nation as well as the leadership of President George W. Bush.

The over-riding theme of the budget, and the President's plan for the future, is that a safer world is a more prosperous world. That's why I'll be discussing both national and economic security here today.

Decisions about how to collect and spend taxpayer dollars – for this is what a budget is – must be made with both caution and vision.

The Fiscal Year 2005 budget proposal is, therefore, a plan that does three core things:

- One: Keeps Americans safe by providing the resources necessary to win the war on terror and protect our homeland;
- Two: Increases the economic security of our citizens as well, by strengthening our economy; and
- Three: Exercises the kind of spending discipline that is required by a government that respects the source of its money (hard-working taxpayers!) and is unwilling to live with a deficit.

Discussions of our budget and our economy are not, and should not, be separate. The two are inextricably connected.

Today, our economy is doing better.

Homeownership is up, unemployment is heading down, and GDP growth has been strong.

This administration came to office when those indicators were not nearly as positive.

The President inherited an economy that was in decline... one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

The President and his administration took these challenges seriously and we have made *serious progress* in changing the economic direction of this country.

The President's tax cuts – passed by you – have worked. They provided the stimulus that was necessary to turn the economic ship around... and they are now encouraging and allowing for the economic growth that is continuing into the future.

- Economic growth in the second half of 2003 was the fastest since 1984;

- New home construction was the highest in almost 20 years;
- Homeownership levels are at historic highs;
- Manufacturing activity is increasing;
- Inflation and interest rates are low;
- Over 360,000 jobs have been created in the past five months;
- Unemployment claims – both initial claims and continuing claims – are well off their peaks last year, indicating improvement in the labor market;
- This Wednesday, the Dow closed at a 32-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: economic growth is robust and will be sustained.

However, there is more to do. We are not, by any means, satisfied.

There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

Our budget addresses that need by continuing to focus on improving our economy.

For example, the President's Jobs for the 21st Century plan, announced in his State of the Union Address, directs the resources of several branches of government toward matching skills with jobs, and helping workers acquire the skills they need to qualify for the jobs in their community.

We can also encourage the creation of jobs by sticking to the President's six-point plan for growth.

That includes making health care more affordable and costs more predictable.

We can do this by passing Association Health Plan legislation that would allow small businesses to pool together to purchase health coverage for workers at lower rates.

We also need to promote and expand the advantages of using health savings accounts ... how they can give workers more control over their health insurance and costs.

And we've got to reduce frivolous and excessive lawsuits against doctors and hospitals. Baseless lawsuits, driven by lottery-minded attorneys, drive up health insurance costs for workers and businesses.

The need to reduce the lawsuit burden on our economy stretches beyond the area of health care. That's why President Bush has proposed, and the House has approved, measures that would allow more class action and mass tort lawsuits to be moved into Federal court -- so that trial lawyers will have a harder time shopping for a favorable court.

These steps are the second key part of the President's pro-jobs, pro-growth plan.

Ensuring an affordable, reliable energy supply is a third part.

We must enact comprehensive national energy legislation to upgrade the Nation's electrical grid, promote energy efficiency, increase domestic energy production, and provide enhanced conservation efforts, all while protecting the environment.

Again, we need Congressional action: we ask that you pass legislation based on the President's energy plan.

Streamlining regulations and reporting requirements are another critical reform element that benefit small businesses, who represent the majority of new job creation: three out of every four net new jobs come from the small-business sector! Let's give them a break wherever we can so they're free to do what they do best: create those jobs.

Opening new markets for American products is another necessary step toward job creation. That's why President Bush recently signed into law new free trade agreements with Chile and Singapore that will enable U.S. companies to compete on a level playing field in these markets for the first time -- and he will continue to work to open new markets for American products and services.

Finally, we've got to enable families and businesses to plan for the future with confidence.

That means making the President's tax relief permanent.

Rate reductions, the increase in the child tax credit and the new incentives for small-business investment – these will all expire in a few years. The accelerated rate reductions that took effect in 2003 will expire at the end of this year. Expiration dates are not acceptable – we want permanent relief.

The ability of American families and businesses to make financial decisions with confidence determines the future of our economy. And without permanent relief, incentives upon which they can count, we risk losing the momentum of the recovery and growth that we have experienced in recent months.

The tax relief is the key stimulus for increased capital formation, entrepreneurship and investment that cause true economic growth.

Budgets work better when the economy is growing… because a growing economy means more jobs. That means more tax revenue… which leads to all-important deficit reduction.

Which leads me to my next area of discussion.

Let me be clear on this:

- The budget deficit that we face today is unwelcome.
- It needs to be addressed.
- The President's budget calls for cutting the deficit in half over the next five years.
- While addressing the deficit, we must remember that it is not *historically* overwhelming.
- It is understandable, given the extraordinary circumstances of recent history. Remember that we are fighting a type of war that we have never fought before. We are fighting an enemy that requires a much broader variety of government resources than anything we've ever confronted. And we began this fight when we were economically wounded.

What's most important to remember is that *we will be able to fight this war and climb out of the deficit.*

We can manage this deficit, and we can cut it in half over the next five years by *controlling spending and growing our economy*.

Three-quarters of the discretionary spending increases during this Administration have been related to the global war on terror and the response to 9/11.

Meanwhile, President Bush has reduced the rate of increase in non-security-related discretionary spending every year he has been in office: to six percent in 2002, five percent in 2003, and to four percent in the current fiscal year.

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The President has been clear on this: younger workers should have the opportunity to build a nest egg by saving part of their Social Security taxes in personal retirement accounts. His vision for the program is economically wise, and it is that we should make the Social Security system a source of ownership for the American people.

Are we dedicating ourselves to increased spending on the war on terror and protecting the homeland? The answer is yes. Yes, without sacrificing other necessities.

And that is because a nation must be safe in order for it to be prosperous.

A nation of entrepreneurs must also be able to plan, and to be relieved of as many burdens as possible, in order to be prosperous.

All of the budget issues and policy proposals that I've discussed today may seem, at times, to be a complicated recipe. But these ingredients combine to make something that is simply put, and is of utmost importance – and that is economic growth.

Growth is the key to every economic problem we confront. That's why we urge other countries to institute pro-growth policies. It's good for them, and it's good for the global economy that we are a significant part of.

Thank you for hearing my testimony today. I'll be happy to take your questions now.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 13, 2004
JS-1172

Treasury and IRS shut down abusive Life Insurance Policies in Retirement Plans

Today, the Treasury Department and the Internal Revenue Service issued guidance to shut down abusive transactions involving specially designed life insurance policies in retirement plans, section "412(i) plans." The guidance designates certain arrangements as "listed transactions" for tax-shelter reporting purposes.

A "section 412(i) plan" is a tax-qualified retirement plan that is funded entirely by a life insurance contract or an annuity. The employer claims tax deductions for contributions that are used by the plan to pay premiums on an insurance contract covering an employee. The plan may hold the contract until the employee dies, or it may distribute or sell the contract to the employee at a specific point, such as when the employee retires.

"The guidance targets specific abuses occurring with section 412(i) plans," stated Assistant Secretary for Tax Policy Pam Olson. "There are many legitimate section 412(i) plans, but some push the envelope, claiming tax results for employees and employers that do not reflect the underlying economics of the arrangements."

"Again and again, we've uncovered abusive tax avoidance transactions that game the system to the detriment of those who play by the rules," said IRS Commissioner Mark W. Everson. "Today's action sends a strong signal to those taking advantage of certain insurance policies that these abusive schemes must stop."

The guidance covers three specific issues. First, a set of new proposed regulations states that any life insurance contract transferred from an employer or a tax-qualified plan to an employee must be taxed at its full fair market value. Some firms have promoted an arrangement where an employer establishes a section 412(i) plan under which the contributions made to the plan, which are deducted by the employer, are used to purchase a specially designed life insurance contract. Generally, these special policies are made available only to highly compensated employees. The insurance contract is designed so that the cash surrender value is temporarily depressed, so that it is significantly below the premiums paid. The contract is distributed or sold to the employee for the amount of the current cash surrender value during the period the cash surrender value is depressed; however the contract is structured so that the cash surrender value increases significantly after it is transferred to the employee. Use of this springing cash value life insurance gives employers tax deductions for amounts far in excess of what the employee recognizes in income. These regulations, which will be effective for transfers made on or after today, will prevent taxpayers from using artificial devices to understate the value of the contract. A revenue procedure issued today along with the proposed regulations provides a temporary safe harbor for determining fair market value.

Second, a new revenue ruling states that an employer cannot buy excessive life insurance (i.e., insurance contracts where the death benefits exceed the death benefits provided to the employee's beneficiaries under the terms of the plan, with the balance of the proceeds reverting to the plan as a return on investment) in order to claim large tax deductions. These arrangements generally will be listed transactions for tax-shelter reporting purposes.

Third, another new revenue ruling states that a section 412(i) plan cannot use differences in life insurance contracts to discriminate in favor of highly paid

employees.

Related Documents:

- Proposed Regulations
- Rev Rul. 2004-20
- Rev Rul. 2004-21
- Rev Proc. 2004-16

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-126967-03]

RIN 1545-BC20

Value of Life Insurance Contracts when Distributed from a Qualified Retirement Plan

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed amendments to the regulations under section 402(a) of the Internal Revenue Code regarding the amount includible in a distributee's income when life insurance contracts are distributed by a qualified retirement plan and the treatment of property sold by a qualified retirement plan to a plan participant or beneficiary for less than fair market value. This document also contains proposed amendments to the regulations under sections 79 and 83 conforming the language in those regulations to the language in the proposed amendments to the section 402(a) regulations. These regulations will affect administrators of, participants in, and beneficiaries of qualified employer plans. These regulations also provide guidance to employers who provide group-term life insurance to their employees that is includible in the gross income of the employees and to employers who transfer life insurance contracts to persons in connection with the performance of services. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written or electronic comments must be received by May 13, 2004. Requests to speak and outlines of topics to be discussed at the public hearing scheduled for June 9, 2004, at 10 a.m., must be received by May 19, 2004.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-126967-03), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-126967-03), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington D.C. Alternatively, taxpayers may submit comments electronically directly to the IRS Internet site at www.irs.gov/regs. The public hearing will be held in the Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, D.C.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed amendments to the section 79 regulations, Betty Clary at (202) 622-6080; concerning the proposed amendments to the section 83 regulations, Robert Misner at (202) 622-6030; concerning the proposed amendments to the 402 regulations, Linda Marshall at (202) 622-6090; concerning submissions and the hearing and/or to be placed on the building access list to attend the hearing, Robin Jones at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 402(a) of the Internal Revenue Code (Code) relating to the amount includible in a distributee's income when a life insurance contract, retirement income contract, endowment contract, or other contract providing life

insurance protection is distributed by a retirement plan qualified under section 401(a) of the Code and to the sale of property by a retirement plan to a plan participant or beneficiary for less than the fair market value of the property. This document also contains proposed amendments to the regulations under sections 79 and 83 relating, respectively, to employer-provided group-term life insurance and life insurance contracts transferred in connection with the performance of services.

Section 402(a) provides generally that any amount actually distributed to any distributee by any employees' trust described in section 401(a) which is exempt from tax under section 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under section 72.

Section 1.402(a)-1(a)(1)(iii) of the current regulations provides, in general, that a distribution of property by a section 401(a) plan shall be taken into account by the distributee at its "fair market value." Section 1.402(a)-1(a)(2) of the regulations provides, in general, that upon the distribution of an annuity or life insurance contract, the "entire cash value" of the contract must be included in the distributee's income. The current regulations do not define "fair market value" or "entire cash value" and questions have arisen regarding the interaction between these two provisions and whether "entire cash value" includes a reduction for surrender charges.

Prohibited Transaction Exemption (PTE) 77-8 (1977-2 C.B. 425), subsequently amended and redesignated as Prohibited Transaction Exemption 92-6, was jointly issued in 1977 by the Department of Labor and the Internal Revenue Service. PTE 77-8 permits an employee benefit plan to sell individual life insurance contracts and annuities to (1) a plan participant insured under such policies, (2) a relative of such

insured participant who is the beneficiary under the contract, (3) an employer any of whose employees are covered by the plan, or (4) another employee benefit plan, for the cash surrender value of the contracts, provided the conditions set forth in the exemption are met.

The preamble to PTE 77-8 (citing Rev. Rul. 59-195; 1959-1 C.B. 18) notes that, for Federal income tax purposes, the value of an insurance policy is not the same as, and may exceed, its cash surrender value, and that a purchase of an insurance policy at its cash surrender value may therefore be a purchase of property for less than its fair market value. The regulations under section 402 do not address the consequences of a sale of property by a section 401(a) plan to a plan participant or beneficiary for less than the fair market value of that property. In this regard, the preamble to PTE 77-8 states that the Federal income tax consequences of such a bargain purchase must be determined in accordance with generally applicable Federal income tax rules but that any income realized by a participant or relative of such participant upon such a purchase under the conditions of PTE 77-8 will not be deemed a distribution from the plan to such participant for purposes of subchapter D of chapter 1 of the Internal Revenue Code (i.e., sections 401 to 424 of the Code) relating to qualified pension, profit-sharing, and stock bonus plans.

Section 79 of the Code generally requires that the cost of group-term life insurance coverage provided by an employer on the life of an employee that is in excess of $50,000 of coverage be included in the income of the employee. Pursuant to §1.79-1(b) of the regulations, under specified circumstances, group-term life insurance may be combined with other benefits, referred to as permanent benefits. A permanent

benefit is defined in §1.79-0 of the regulations as an economic value extending beyond one policy year (for example, a paid-up or cash surrender value) that is provided under a life insurance policy. The regulations further provide that certain features are not permanent benefits, including (a) a right to convert (or continue) life insurance after group life insurance coverage terminates, (b) any other feature that provides no economic benefit (other than current insurance protection) to the employee, and (c) a feature under which term life insurance is provided at a level premium for a period of five years or less.

Permanent benefits provided to an employee are subject to taxation under rules described in §1.79-1(d) of the regulations. Under those rules, the cost of the permanent benefits, reduced by the amount paid for those benefits by the employee, is included in the employee's income. The regulations provide the cost of the permanent benefits can be no less than an amount determined under a formula set forth in the regulations. One of the factors used in this formula is "the net level premium reserve at the end of that policy year for all benefits provided to the employee by the policy or, if greater, the cash value of the policy at the end of that policy year."

Section 83(a) provides that when property is transferred to any person in connection with the performance of services, the service provider must include in gross income (as compensation income) the excess of the fair market value of the property, determined without regard to lapse restrictions, and determined at the first time that the transferee's rights in the property are either transferable or not subject to a substantial risk of forfeiture, over the amount (if any) paid for the property. Section 1.83-3(e) of the regulations generally provides that in the case of "a transfer of a life insurance contract,

retirement income contract, endowment contract, or other contract providing life insurance protection, only the cash surrender value of the contract is considered to be property."

In TD 9092, published in the **Federal Register** on September 17, 2003 (68 FR 54336), relating to split-dollar life insurance arrangements, §1.83-3(e) was amended to add the following sentence: "Notwithstanding the previous sentence, in the case of a transfer of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, or any undivided interest therein, that is part of a split-dollar life insurance arrangement (as defined in §1.61-22(b)(1) or (2)) that is entered into, or materially modified (within the meaning of §1.61-22(j)(2)), after September 17, 2003, the policy cash value and all other rights under such contract (including any supplemental agreements thereto and whether or not guaranteed), other than current life insurance protection, are treated as property for purposes of this section."

Explanation of Provisions

A. Overview

These proposed amendments to the regulations under section 402(a) clarify that the requirement that a distribution of property must be included in the distributee's income at fair market value is controlling in those situations where the existing regulations provide for the inclusion of the entire cash value. Thus, these proposed regulations provide that, in those cases where a qualified plan distributes a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, the fair market value of such a contract (i.e., the

value of all rights under the contract, including any supplemental agreements thereto and whether or not guaranteed) is generally included in the distributee's income and not merely the entire cash value of the contracts.

These proposed regulations also provide that if a qualified plan transfers property to a plan participant or beneficiary for consideration that is less than the fair market value of the property, the transfer will be treated as a distribution by the plan to the participant or beneficiary to the extent the fair market value of the distributed property exceeds the amount received in exchange. Thus, in contrast to the statement to the contrary in the preamble to PTE 77-8, any bargain element in the sale would be treated as a distribution under section 402(a). It is also intended that any bargain element would be treated as a distribution for other purposes of the Code, including the limitations on in-service distributions from certain qualified retirement plans and the limitations of section 415.

These proposed regulations also amend the current regulations under sections 79 and 83 to clarify that fair market value is also controlling with respect to life insurance contracts under those sections and, thus, that all of the rights under the contract (including any supplemental agreements thereto and whether or not guaranteed) must be considered in determining that fair market value. With respect to section 79, these proposed regulations would amend §1.79-1(d) to remove the term cash value from the formula for determining the cost of permanent benefits and substitute the term fair market value. With respect to section 83, these proposed regulations would amend §1.83-3(e) generally to apply the definition of property for new split-dollar life insurance arrangements to all situations involving the transfer of life insurance contracts. Section

83(a) requires that the excess of the fair market value of the property over the amount paid for the property be included in income. The current definition of property outside the context of a split-dollar life insurance arrangement may lead taxpayers to believe that it is appropriate upon receiving a transfer of a life insurance contract to include only its cash surrender value on the day of the transfer when, due to supplemental agreements, the fair market value of the transferred property is much greater. The purpose of the changes to these regulations is to clarify that, unless specifically excepted from the definition of permanent benefits or fair market value, the value of all features of a life insurance policy providing an economic benefit to a service provider (including, for example, the value of a springing cash value feature) must be included in determining the employee's income.

The proposed regulations will not affect the relief granted by the provisions of Section IV, paragraph 4 of Notice 2002-8 (2002-1 C.B. 398) to the parties to any insurance contract that is part of a pre-January 28, 2002, split-dollar life insurance arrangement. Also, consistent with the effective date of the final split-dollar life insurance regulations, §1.61-22, these proposed regulations will not apply to the transfer of a life insurance contract which is part of a split-dollar life insurance arrangement entered into on or before September 17, 2003, and not materially modified after that date. However, taxpayers are reminded that, in determining the fair market value of property transferred under section 83, lapse restrictions (such as life insurance contract surrender charges) are ignored.

B. Determination of Fair Market Value

As noted above, §1.402(a)-1(a)(1)(iii) does not define fair market value. In Rev. Rul. 59-195, the Service ruled that, in situations similar to those in which an employer purchases and pays the premiums on an insurance policy on the life of one of its employees and subsequently sells such policy, on which further premiums must be paid, the value of such policy for computing taxable gain in the year of purchase should be determined under the method of valuation prescribed in §25.2512-6 of the Gift Tax Regulations. Under this method, the value of such a policy is not its cash surrender value but the interpolated terminal reserve at the date of sale plus the proportionate part of any premium paid by the employer prior to the date of the sale which is applicable to a period subsequent to the date of the sale. Section 25.2512-6 of the Gift Tax Regulations also provides that if "because of the unusual nature of the contract such approximation is not reasonably close to the full value, this method may not be used." Thus, this method may not be used to determine the fair market value of an insurance policy where the reserve does not reflect the value of all of the relevant features of the policy.

In Q&A-10 of Notice 89-25 (1989-1 C.B. 662), the IRS addressed the question of what amount is includible in income under section 402(a) when a participant receives a distribution from a qualified plan that includes a life insurance policy with a value substantially higher than the cash surrender value stated in the policy. The Notice noted the practice of using cash surrender value as fair market value for these purposes and concluded that this practice is not appropriate where the total policy reserves, including life insurance reserves (if any) computed under section 807(d), together with

any reserves for advance premiums, dividend accumulations, etc., represent a much more accurate approximation of the policy's fair market value.

Since Notice 89-25 was issued, life insurance contracts have been marketed that are structured in a manner which results in a temporary period during which neither a contract's reserves nor its cash surrender value represent the fair market value of the contract. For example, some life insurance contracts may provide for large surrender charges and other charges that are not expected to be paid because they are expected to be eliminated or reversed in the future (under the contract or under another contract for which the first contract is exchanged), but this future elimination or reversal is not always reflected in the calculation of the contract's reserve. If such a contract is distributed prior to the elimination or reversal of those charges, both the cash surrender value and the reserve under the contract could significantly understate the fair market value of the contract. Thus, in some cases, it would not be appropriate to use either the net surrender value (i.e. the contract's cash value after reduction for any surrender charges) or, because of the unusual nature of the contract, the contract's reserves to determine the fair market value of the contract. Accordingly, Q&A-10 of Notice 89-25 should not be interpreted to provide that a contract's reserves (including life insurance reserves (if any) computed under section 807(d), together with any reserves for advance premiums, dividend accumulations, etc.) are always an accurate representation of the contract's fair market value.

For example, it would not be appropriate to use a contract's reserve or the net surrender value of the contract as fair market value at the time of distribution if under that contract those amounts are significantly less than the aggregate of: (1) the

premiums paid from the date of issue through the date of distribution, plus (2) any amounts credited (or otherwise made available) to the policyholder with respect to those premiums (including interest, dividends, and similar income items), or, in the case of variable contracts, all adjustments made with respect to the premiums paid during that period that reflect investment return and the current market value of segregated asset accounts, minus (3) reasonable mortality charges and reasonable charges (other than mortality charges) actually charged from the date of issue to the date of distribution and expected to be paid.

The following example provides an illustration of a contract where it would not be appropriate to use a contract's reserve or its net surrender value as its fair market value:

A participates in a plan intended to satisfy the requirements of section 401(a). In Year 1, the plan acquires a life insurance contract on A's life that is not a variable contract and with a face amount of $1,400,000. In that year and for the next four years, the plan pays premiums of $100,000 per year on the contract. The contract provides for a surrender charge that is fixed for the first five years of the contract and decreases ratably to zero at the end of ten years. The contract also imposes reasonable mortality and other charges as defined by section 7702(c)(3)(B)(i) and (ii) of the Code.

The contract provides a stated cash surrender value for each of the first ten years (the first five years are guaranteed), as set forth in the table below. The reserves under the contract, including life insurance reserves and reserves for advance premiums, dividend accumulations, etc. (calculated using the rules in section 807(d) of the Code) at the end of the fifth year are $150,000.

Year	Premium	Net Surrender Value	Cash Value Determined without Reduction for Surrender Charges
1	$100,000		
2	$100,000		
3	$100,000		
4	$100,000		
5	$100,000	$100,000	$450,000
6		$195,000	$475,000
7		$290,000	$500,000
8		$385,000	$525,000
9		$480,000	$550,000
10		$575,000	$575,000

At the end of Year 5, A retired and received a distribution of the insurance contract that was purchased on his life.

These regulations clarify that the contract is included in A's income at its fair market value rather than the $100,000 cash surrender value. Furthermore, A could not treat the $150,000 reserve as of the end of the fifth year as the fair market value, because this amount is less than the amount a willing buyer would pay a willing seller

for such a contract, with neither party being under a compulsion to buy and sell and both having reasonable knowledge of the relevant facts.

Proposed Effective Dates

The amendments to §1.402(a)-1(a)(2) of the regulations are proposed to be applicable to any distribution of a transferable retirement income, endowment, or other life insurance contract occurring on or after February 13, 2004. The amendment to §1.79-1 is proposed to be applicable to permanent benefits provided on or after February 13, 2004. The amendment to §1.83-3(e) is proposed to be applicable to any transfer occurring on or after February 13, 2004. The amendments to §1.402(a)-1(a)(1)(iii) of the regulations are proposed to be applicable to any transfer of property by a plan to a plan participant or beneficiary for less than fair market value where the transfer occurs on or after the date of publication in the **Federal Register** of the final regulations adopting these amendments. Taxpayers may rely upon these proposed regulations for guidance pending the issuance of final regulations.

Interim Guidance for Determining Fair Market Value

The IRS and the Treasury recognize that taxpayers could have difficulty determining the fair market value of a life insurance contract after the clarification in this preamble that Notice 89-25 should not be interpreted to provide that a contract's reserves (including life insurance reserves (if any) computed under section 807(d), together with any reserves for advance premiums, dividend accumulations, etc.) are always an accurate representation of the contract's fair market value. Accordingly, in connection with this guidance, the IRS has issued Rev. Proc 2004-16 (2004-10 IR.B.), which provides interim rules under which the cash value (without reduction for surrender

charges) of a life insurance contract distributed from a qualified plan may be treated as the fair market value of that contract. The interim rules in Rev. Proc. 2004-16, permit the use of values that should be readily available from insurance companies, because the cash value (without reduction for surrender charges) is an amount that, in the case of a flexible insurance contract (including a variable contract), is generally reported in policyholder annual statements, and in the case of traditional insurance contracts, is fixed at issue and provided in the insurance contract.

Under those interim rules, a plan may treat the cash value (without reduction for surrender charges) as the fair market value of a contract at the time of distribution provided such cash value is at least as large as the aggregate of: (1) the premiums paid from the date of issue through the date of distribution, plus (2) any amounts credited (or otherwise made available) to the policyholder with respect to those premiums, including interest, dividends, and similar income items (whether under the contract or otherwise), minus (3) reasonable mortality charges and reasonable charges (other than mortality charges), but only if those charges are actually charged on or before the date of distribution and are expected to be paid.

In those cases where the contract is a variable contract (as defined in section 807(d)) a plan may treat the cash value (without reduction for surrender charges) as the fair market value of the contract at the time of distribution provided such cash value is at least as large as the aggregate of: (1) the premiums paid from the date of issue through the date of distribution, plus (2) all adjustments made with respect to those premiums during that period (whether under the contract or otherwise) that reflect investment return and the current market value of segregated asset accounts, minus (3) reasonable

mortality charges and reasonable charges (other than mortality charges), but only if those charges are actually charged on or before the date of distribution and are expected to be paid.

Applying those interim rules to the example above, A could treat the cash value (without reduction for surrender charges) of $450,000 as the fair market value of the contract as of the end of the fifth year, because, in this example, that amount exceeds the aggregate of the five $100,000 premiums ($500,000), plus the amounts credited to A with respect to those premiums, minus the reasonable mortality and other charges actually imposed and expected to be paid.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury

Department specifically request comments on the clarity of the proposed regulations and how they may be made easier to understand. In addition, the Treasury Department and the IRS specifically request comments regarding the interim rules set forth in Rev. Proc. 2004-16 and proposals for appropriate permanent methods for valuing life insurance contracts when distributed from qualified retirement plans and for valuing such contracts for purposes of sections 79 and 83, including appropriate discounts which take into account the probability that contracts will be surrendered during the period during which surrender charges apply. The IRS and the Treasury are also reviewing other types of contracts, such as annuities, which have cash surrender value but where that cash surrender value may not reflect the fair market value of the contracts. Accordingly, the IRS and the Treasury also request comments regarding the valuation of these other contracts. All comments will be available for public inspection and copying.

A public hearing has been scheduled for Wednesday, June 9, 2004, at 10 a.m. in the auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must use the main building entrance on Constitution Avenue. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For more information about having your name placed on the list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written (signed original and eight (8)

copies) or electronic comments and an outline of the topics to be discussed and the time to be devoted to each topic by Wednesday, May 19, 2004. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal authors of these regulations are Robert M. Walsh, Employee Plans, Tax Exempt and Government Entities Division, and Linda Marshall, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury participated in the development of these regulations.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1 -- INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read, in part, as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2 Section 1.79-1, paragraph (d)(3) is revised to read as follows:

<u>§1.79-1 Group-term life insurance -- general rules</u>.

* * * * *

(d) * * *

(3) Formula for determining deemed death benefit. The deemed death benefit (DDB) at the end of any policy year for any particular employee is equal to:

R/Y

where--

R is the net level premium reserve at the end of that policy year for all benefits provided to the employee by the policy or, if greater, the fair market value of the policy at the end of that policy year; and

Y is the net single premium for insurance (the premium for one dollar of paid-up, whole life insurance) at the employee's age at the end of that policy year.

* * * * *

Par. 3. In §1.83-3, paragraph (e), the last two sentences are revised to read as follows:

§1.83-3 Meaning and use of certain terms.

* * * * *

(e) * * * In the case of a transfer of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, or any undivided interest therein, the policy cash value and all other rights under such contract (including any supplemental agreements thereto and whether or not guaranteed), other than current life insurance protection, are treated as property for purposes of this section. However, in the case of the transfer of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, which was part of a split-dollar arrangement (as defined in §1.61-22(b)) entered into (as defined in §1.61-22(j)) on or before September 17, 2003,

and which is not materially modified (as defined in §1.61-22(j)(2)) after September 17, 2003, only the cash surrender value of the contract is considered to be property.

* * * * *

Par. 4. Section 1.402(a)-1 is amended by:

1. Revising paragraph (a)(1)(iii).

2. Revising the last two sentences of paragraph (a)(2).

The revisions read as follows:

§1.402(a)-1 Taxability of beneficiary under a trust which meets the requirements of section 401(a).

(a)* * * (1) * * *

(iii) Except as provided in paragraph (b) of this section, a distribution of property by a trust described in section 401(a) and exempt under section 501(a) shall be taken into account by the distributee at its fair market value. In the case of a distribution of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, or any interest therein, the policy cash value and all other rights under such contract (including any supplemental agreements thereto and whether or not guaranteed) are included in determining the fair market value of the contract. In addition, where a trust described in section 401(a) and exempt under section 501(a) transfers property to a plan participant or beneficiary in exchange for consideration and where the fair market value of the property transferred exceeds the amount received by the trust, then the excess of the fair market value of the property transferred by the trust over the amount received by the trust is treated as a distribution by the trust to the distributee.

* * * * *

(2)* * * If, however, the contract distributed by such exempt trust is a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, the fair market value of such contract at the time of distribution must be included in the distributee's income in accordance with the provisions of section 402(a), except to the extent that, within 60 days after the distribution of such contract, all or any portion of such value is irrevocably converted into a contract under which no part of any proceeds payable on death at any time would be excludable under section 101(a) (relating to life insurance proceeds). If the contract distributed by such trust is a transferable annuity contract, a life insurance contract, a retirement income contract, endowment contract, or other contract providing life insurance protection (whether or not transferable), then notwithstanding the preceding

sentence, the fair market value of the contract is includible in the distributee's gross income, unless within such 60 days such contract is also made nontransferable.

* * * * *

Mark E. Matthews,

Deputy Commissioner for Services and Enforcement.

Part I

Section 404.--Deduction for Contributions of an Employer to an Employees' Trust or Annuity Plan and Compensation Under a Deferred Payment Plan

(Also, §§ 401, 412, 6011, 6111, 6112; §§ 26 CFR 1.401-1, 1.412(i)-1, 1.6011-4, 301.6111-2, 301.6112-1.)

Rev. Rul. 2004-20

ISSUES

Issue 1: Can a qualified pension plan be a plan described in § 412(i) of the Internal Revenue Code if the plan holds life insurance contracts and annuity contracts for the benefit of a participant that provide for benefits at normal retirement age in excess of the participant's benefits at normal retirement age under the terms of the plan?

Issue 2: If a qualified pension plan holds life insurance contracts providing for life insurance on a participant's life in excess of the participant's death benefit under the terms of the plan, are contributions for premiums for such excess life insurance coverage currently deductible by the employer?

FACTS

Situation 1

Employer M maintains Plan A, a defined benefit plan that is funded solely by life insurance contracts and annuities with level annual premiums for each participant commencing with the date the individual becomes a participant in the plan (or, in the case of an increase in benefits, commencing at the time the increase becomes effective) and ending with the individual's attainment of normal retirement age. Plan A is intended to be a

plan described in § 412(i). The amounts that will be accumulated under the insurance contracts and annuity contracts for the benefit of a participant at normal retirement age, assuming premiums are paid and determined by applying annuity purchase rates guaranteed under the contracts, will provide for benefits in excess of the participant's benefits at normal retirement age under the terms of the plan.

Situation 2

Employer N maintains Plan B. With respect to Participant P, Plan B provides a death benefit that meets the definition of an incidental death benefit under § 1.401-1(b)(1)(i) of the Income Tax Regulations. The assets of Plan B include life insurance contracts on the life of Participant P with a face amount in excess of Participant P's death benefit under Plan B. Premiums with respect to Participant P include an annual premium for the waiver of the entire premium payment if Participant P becomes disabled. Upon the death of a covered employee, the portion of the proceeds of the life insurance contract that exceeds the death benefit payable to Participant P's beneficiary under the plan is applied to the payment of premiums under the plan with respect to other participants.

LAW AND ANALYSIS

Section 412 sets forth minimum funding requirements for qualified pension plans. Section 412(i) describes certain insurance contract plans that are exempt under § 412(h)(2) from the minimum funding requirements of § 412 (section 412(i) plans). Under § 411(b)(1)(F), a plan that is funded exclusively by the purchase of insurance contracts and satisfies the requirements of § 412(i)(2) and (3) satisfies the accrual requirements of § 411(b) if an employee's accrued benefit as of any applicable date is not less than the

cash surrender value his life insurance contracts would have on that applicable date if the requirements of § 412(i)(4) through (6) were satisfied.

A section 412(i) plan must be funded by the purchase of individual or group insurance contracts. Section 412(i)(2) requires contracts held by a section 412(i) plan to provide for level annual premium payments to be paid commencing with the date the individual became a participant in the plan (or, in the case of an increase in benefits, commencing at the time the increase becomes effective) and extending not later than the retirement age for each individual participating in the plan. Section 412(i)(3) requires benefits provided under a section 412(i) plan to be equal to the benefits provided under each contract at normal retirement age under the plan.

Under § 1.412(i)-1(b)(2)(iii), the benefits for each participant provided under a section 412(i) plan that holds individual insurance contracts must be equal to the benefits provided under the participant's individual contracts at the participant's normal retirement age under the plan. Furthermore, under § 1.412(i)-1(b)(2)(iv), the benefits provided by the plan for each individual participant must be guaranteed by the life insurance company issuing the individual contracts to the extent premiums have been paid.

Section 404(a)(1)(A)(i) provides that the amount necessary to satisfy the minimum funding requirement under § 412 is deductible even if it is greater than the amount determined under § 404(a)(1)(A)(ii) or (iii), whichever is applicable with respect to the plan.

The alternative limit determined under § 404(a)(1)(A)(ii) is the amount necessary to provide the remaining unfunded cost of all participants' past and current service credits as a level amount, or as a level percentage of compensation, over the remaining future service

of each participant. However, if the remaining unfunded cost with respect to any three individuals is more than 50 percent of all remaining unfunded cost, the amount attributable to those individuals is distributed over a period of at least five years.

The alternative limit determined under § 404(a)(1)(A)(iii) is the normal cost of the plan plus, if past service or other supplementary pension or annuity credits are provided by the plan, the amount necessary to amortize the unfunded costs attributable to those credits in equal annual payments over 10 years.

Under § 1.404(a)-6(a)(2) of the Income Tax Regulations, the normal cost for any year is defined as the amount actuarially determined which would be required as a contribution by the employer in such year to maintain the plan if the plan had been in effect from the beginning of service of each then included employee and if such costs for prior years had been paid and all assumptions as to interest, mortality, time of payment, etc., had been fulfilled.

Section 1.404(a)-3(b) provides that in no event shall the limitations under § 404(a)(1) for pension or annuity plans exceed costs based on assumptions and methods that are reasonable in view of the funding medium and reasonable expectations as to the effects of mortality, interest, and other pertinent factors.

Section 1.404(a)-14 provides rules for determining the deductible limits under § 404(a)(1)(A)(i), (ii), and (iii). The regulations provide in general that the limit on deductible amounts contributed for an employer's taxable year is based on the amounts determined for purposes of § 412 for the applicable plan year or years.

Section 404(a)(1)(E) provides that an amount contributed to a plan that would otherwise be deductible, but that exceeds the limitations of § 404(a)(1), is deductible in future years to the extent of the difference between the amount contributed and the maximum amount deductible for each succeeding year under § 404(a)(1).

Section 4972 generally imposes a 10-percent excise tax on nondeductible contributions to a qualified plan, including nondeductible contributions carried over from preceding years.

Rev. Rul. 94-75, 1994-2 C.B. 59, discusses the tax consequences of converting a qualified defined benefit plan that is not a section 412(i) plan to a section 412(i) plan, and holds that the deductible limit under § 404(a)(1)(A)(iii) applies to a section 412(i) plan.

Rev. Rul. 55-748, 1955-2 C.B. 234, discusses the deductibility of contributions to a qualified plan that are used to pay life insurance premiums attributable to the life insurance benefits of retirement income contracts purchased with respect to employees by the trust, the proceeds of which, upon the death of an employee, are payable to the trustee and are held by the trustee for application to payment of subsequent premiums on similar contracts on behalf of other employees. Rev. Rul. 55-748 holds that the part of the employer's contribution attributable to the purchase of life insurance benefits, which, when they become payable, are applicable to the reduction of subsequent employer contributions to the plan are not considered as a cost of the pension plan for the purpose of determining the limitation on deductions under § 404(a)(1)(A), (B), and (C) of the Code (the predecessor provisions to current §§ 404(a)(1)(A)(i), (ii), and (iii)) for the year in which such contributions are paid, and cannot be deducted as such. Rev. Rul. 55-748 further provides

that contributions attributable to such insurance benefits, not otherwise determined, may be determined by applying the rates provided in Rev. Rul. 55-747, 1955-2 C.B. 228, to the amounts of insurance that would revert to the trust in the event of death of the insured employee in the year for which the premiums are paid. In later years, if an employer for any reason, such as the receipt by the trustee of life insurance proceeds under a retirement income contract because of the death of an employee, which proceeds were applied to the payment of premiums on similar contracts for the benefit of other employees, contributes to the trust a sum less than the maximum deduction permitted for that year under § 404(a)(1)(A), (B), or (C), Rev. Rul. 55-748 provides that the employer may deduct in that year, in addition to this current contribution, the contributions made in prior years and not then deductible because they were attributable to that part of the retirement income contracts that would provide life insurance payable to the trustee, to the extent of the difference between his current contribution and his maximum deduction permitted under § 404(a)(1)(A), (B), or (C).

Rev. Rul. 55-747 provided a table to be used in computing the premiums to be included in the income of an employee on account of current life insurance protection provided for the employee under a life or endowment insurance contract held by an employees' trust qualified under § 401(a).

Rev. Rul. 66-110, 1966-1 C.B. 12, provided that the current published premium rates charged by an insurer for individual 1-year term life insurance available to all standard risks may be used for determining the cost of insurance in connection with individual policies issued by the same insurer and held by an employees' trust qualified under

§ 401(a). In addition, Rev. Rul. 66-110 extended the table of premiums set forth in Rev. Rul. 55-747 to cover additional ages.

Rev. Rul. 67-154, 1967-1 C.B. 11, amplified Rev. Rul. 66-110 and held that, where an insurer published one-year term insurance rates lower than those set forth in Rev. Rul. 55-747, but those rates were applicable only under a dividend option whereby term insurance may be purchased with dividends on existing policies and were lower than the insurer's published rates for initial insurance available to all standard risks, those rates could not be used in place of the rates set forth in Rev. Rul. 55-747 in determining the cost of insurance under a trust described in § 401(a).

Notice 2001-10, 2001-1 C.B. 459, revoked Rev. Rul. 55-747, and provided a new table (Table 2001) to be used in valuing term life insurance coverage provided to an employee. Under Notice 2001-10, taxpayers could continue to use the rates set forth in Rev. Rul. 55-747 for purposes of determining the value of current life insurance protection provided under a qualified retirement plan for taxable years ending on or before December 31, 2001. In addition, Notice 2001-10 provided generally that taxpayers could continue to determine the value of current life insurance protection by using the insurer's lower published rates available to standard risks as provided in Rev. Rul. 66-110. However, for periods after December 31, 2003, Notice 2001-10 sets forth certain additional conditions on the use of the insurer's published rates.

Notice 2002-8, 2002-1 C.B. 398, revokes Notice 2001-10. Under Notice 2002-8, Rev. Rul. 55-747 remains revoked; however, taxpayers can use the rates set forth in Rev. Rul. 55-747 for purposes of determining the value of current life insurance protection

provided under a qualified retirement plan for taxable years ending on or before December 31, 2001. Notice 2002-8 republishes Table 2001 and provides that Table 2001 can be used to determine the value of current life insurance protection on a single life that is provided under a qualified plan for arrangements entered into before the effective date of future guidance. In addition, paragraph 3 of Section III of Notice 2002-8 placed conditions on the use of the insurer's lower published rates under Rev. Rul. 66-110, as amplified by Rev. Rul. 67-154, for periods after December 31, 2003, with respect to arrangements entered into after January 28, 2002.

Rev. Rul. 2003-105, 2003-40 I.R.B. 696, obsoleted Rev. Rul. 66-110 for arrangements entered into after September 17, 2003, except as provided in paragraph 3 of Section III of Notice 2002-8. Accordingly, Rev. Rul. 66-110, as amplified by Rev. Rul. 67-154, remains in effect until future guidance is issued for life insurance provided under a qualified retirement plan, subject to the conditions provided by Notice 2002-8 with respect to arrangements entered into after January 28, 2002.

Section 1.401-1(b)(1)(i) provides that a pension plan within the meaning of § 401(a) is a plan established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to employees over a period of years, usually for life, after retirement. A pension plan may also provide for the payment of incidental death benefits through insurance or otherwise.

Rev. Rul. 74-307, 1974-2 C.B. 126, holds that preretirement death benefits under a qualified pension plan are considered incidental death benefits within the meaning of § 1.401-1(b)(1)(i) if less than 50 percent of the employer contribution credited to each

participant's account is used to purchase ordinary life insurance policies on the participant's life, or if the total death benefit before normal retirement date does not exceed the greater of (a) the proceeds of ordinary life insurance policies providing a death benefit of 100 times the anticipated monthly normal retirement benefit, or (b) the sum of (i) the reserve under the ordinary life insurance policies plus (ii) the participant's account in the auxiliary fund. See also Rev. Rul. 68-453, 1968-2 C.B. 163.

Rev. Rul. 81-162, 1981-1 C.B. 169, holds that a plan established by an employer that provides employees only such benefits as are afforded through the purchase of ordinary life insurance contracts (other than retirement income contracts), which are converted to life annuities at normal retirement age, does not constitute a pension plan within the meaning of § 401(a). Rev. Rul. 81-162 provides that the primary purpose of such a life insurance contract is to provide life insurance protection, and the reserve accumulated thereon is a result of premium payments being made on a level basis. Rev. Rul. 81-162 reasons that such reserve will provide a relatively small retirement annuity in comparison with the annuity that a retirement income contract of the same face amount will provide. Therefore, Rev. Rul. 81-162 concludes that a plan providing only for the purchase of ordinary life insurance contracts (other than retirement income contracts) is not primarily for the payment of benefits to employees over a period of years after retirement. This analysis would not apply, however, if the death benefit payable to the beneficiary under the plan were limited to an incidental death benefit, with the remaining benefit payable to the plan.

In Situation 1, Plan A is not a plan described in § 412(i) because the participant's benefit under Plan A payable at normal retirement age is not equal to the amount provided at normal retirement age with respect to the contracts held on behalf of the participant, and thus, Plan A fails to satisfy the requirements of § 412(i)(3). Accordingly, Plan A is subject to the requirements of § 412, with charges and credits to the funding standard account determined using the reasonable funding method selected for the plan under generally applicable rules, and using reasonable actuarial assumptions. Such reasonable funding method and such reasonable actuarial assumptions are also used to determine the deductible amount of contributions under the generally applicable rules of § 404(a). In addition, the exception from the accrual rules that applies to § 412(i) plans under § 411(b)(1)(F) does not apply to Plan A.

In Situation 2, the fact that the life insurance contracts on the life of Participant P provide for death benefits in excess of the death benefits under the plan would not cause Plan B to fail to satisfy the requirements to be a plan described in § 412(i), if Plan B otherwise met those requirements. Similarly, the fact that the life insurance contracts on the life of Participant P provide for death benefits that would fail to satisfy the incidental benefit rule of § 1.401-1(b)(1)(i) if payable to Participant P's beneficiary under the plan does not cause Plan B to fail to satisfy the incidental death benefit rule of § 1.401-1(b)(1)(i) because those excess death benefits under the life insurance contracts are not payable to Participant P's beneficiary under the plan. However, a portion of Employer N's contributions under Plan B is attributable to the purchase of life insurance coverage held by Plan B that is in excess of the incidental death benefit payable under Plan B. Under Rev.

Rul. 55-748, the portion of Employer N's contributions that is attributable to such excess life insurance coverage does not constitute normal cost, and is not deductible as part of normal cost for the taxable year in which contributed. Rather, that portion of Employer N's contributions is used to provide a source of funds to pay future premiums (i.e., premiums on other participants) that will come due after the death of Participant P. Accordingly, the nondeductible portion of Employer N's contributions under Plan B that is paid for life insurance protection for Participant P is carried over pursuant to the rules of § 404(a)(1)(E) to be treated as contributions under the rules of § 404(a)(1)(E) in later years and deductible when the employer contributions are less than the maximum deductible limit (e.g., in years in which excess death benefits under Plan B are used to satisfy Employer N's obligation to pay future premiums on other participants). Similarly, Employer N's contributions to pay premiums for the disability waiver for Participant P do not constitute normal cost, and are not deductible as part of normal cost for the taxable year in which contributed. Rather, that portion of Employer N's contributions is used to provide a source of funds to pay future premiums that will come due after Participant P becomes disabled. Accordingly, the nondeductible portion of Employer N's contributions under Plan B that is paid for the disability waiver for Participant P is carried over pursuant to the rules of § 404(a)(1)(E) to be treated as contributions under the rules of § 404(a)(1)(E) in later years and deductible when the employer contributions are less than the maximum deductible limit (e.g., if and when Participant P becomes disabled).

In general, the premiums for excess life insurance coverage that are not currently part of normal cost under § 404(a)(1)(A) are determined in a manner consistent with total

premiums under the contract (i.e., must be spread in a level manner over the premium payment period). However, if the premiums for the life insurance contracts covering a participant are level annual premiums payable beginning with the participant's participation in the plan and ending at the participant's normal retirement age, this excess amount can be determined by applying the appropriate term cost factors to the excess term coverage. Nondeductible contributions are subject to the excise tax of § 4972 as provided thereunder. In determining the amount of premiums for excess life insurance coverage, Table 2001 is applicable for taxable years ending after December 31, 2001, and the table set forth in Rev. Rul. 55-747 is used for earlier periods. In addition, the current published premium rates charged by an insurer for individual 1-year term life insurance available to all standard risks as described in Rev. Rul. 66-110, as amplified by Rev. Rul. 67-154, can be used for taxable years ending on or before December 31, 2003. For arrangements entered into on or before January 28, 2002, such current published premium rates can continue to be used for periods ending after December 31, 2003. However, for arrangements entered into after January 28, 2002, such current published premium rates can continue to be used for periods ending after December 31, 2003 only if the additional requirements of Notice 2002-8 are satisfied.

HOLDING

A qualified pension plan cannot be a section 412(i) plan if the plan holds life insurance contracts and annuity contracts for the benefit of a participant that provide for benefits at normal retirement age in excess of the participant's benefits at normal retirement age under the terms of the plan.

Employer contributions under a qualified defined benefit plan that are used to purchase life insurance coverage for a participant in excess of the participant's death benefit provided under the plan are not fully deductible when contributed, but are carried over to be treated as contributions in future years and deductible in future years when other contributions to the plan that are taken into account for the taxable year are less than the maximum amount deductible for the year pursuant to the limits of § 404.

LISTED TRANSACTIONS

Transactions that are the same as, or substantially similar to, the transaction described in Situation 2 of this revenue ruling are identified as "listed transactions" for purposes of § 1.6011-4(b)(2) of the Income Tax Regulations and § 301.6111-2(b)(2) and § 301.6112-1(b)(2) of the Procedure and Administration Regulations effective February 13, 2004, the date this revenue ruling was released to the public, provided that the employer has deducted amounts used to pay premiums on a life insurance contract for a participant with a death benefit under the contract that exceeds the participant's death benefit under the plan by more than $100,000.

It should be noted that, independent of any classification as "listed transactions" for purposes of §§ 1.6011-4(b)(2), 301.6111-2(b)(2), and 301.6112-1(b)(2) of the regulations, arrangements that are the same as, or substantially similar to, the arrangements described in this notice may already be subject to the disclosure requirements of § 6011 of the Code, the tax shelter registration requirements of § 6111, or the list maintenance requirements of § 6112 (§§ 1.6011-4, 301.6111-1T, 301.6111-2, and 301.6112-1).

Persons who are required to satisfy the registration requirement of §§ 6111 of the Code with respect to the arrangements described in this notice and who fail to do so may be subject to the penalty under § 6707(a). Persons who are required to satisfy the list-keeping requirement of § 6112 with respect to the arrangements and who fail to do so may be subject to the penalty under § 6708(a). In addition, the Service may impose penalties on participants in these arrangements or substantially similar arrangements, including the accuracy-related penalty under § 6662.

EFFECT ON OTHER RULINGS

Rev. Rul. 55-748 is modified and superseded.

DRAFTING INFORMATION

The principal authors of this revenue ruling are Larry Isaacs of the Employee Plans, Tax Exempt and Government Entities Division, and Linda Marshall of the Office of the Division Counsel/Associate Chief Counsel, Tax Exempt and Government Entities. For further information regarding this revenue procedure, please contact the Employee Plans' taxpayer assistance telephone service at 1-877-829-5500 (a toll-free number) between the hours of 8:00 a.m. and 6:30 p.m. Eastern Time, Monday through Friday. Mr. Isaacs may be reached at (202) 283-9888, and Ms. Marshall may be reached at (202) 622-6090 (not toll-free numbers).

Part I

Section 401.--Qualified pension, profit-sharing, and stock bonus plans

26 CFR 1.401(a)(4)-4: Nondiscriminatory availability of benefits, rights, and features

Rev. Rul. 2004-21

ISSUE

Does a plan that is funded, in whole or in part, with life insurance contracts satisfy the requirements of § 401(a)(4) of the Internal Revenue Code prohibiting discrimination in favor of highly compensated employees where: (1) highly compensated employees are permitted, prior to distribution of retirement benefits, to purchase life insurance contracts from the plan at cash surrender value; and (2) any rights under the plan for nonhighly compensated employees to purchase life insurance contracts from the plan prior to distribution of retirement benefits are not of inherently equal or greater value than the purchase rights of highly compensated employees?

FACTS

Employer M maintains Plan A, a retirement plan that is intended to be a qualified plan under § 401(a). Plan A provides an incidental death benefit within the meaning of § 1.401-1(b)(1)(i) of the Income Tax Regulations for each participant, and holds a life insurance contract on the life of each participant to fund that incidental death benefit. Before distributions to a participant under Plan A commence, each participant is offered the opportunity to purchase the life insurance contract under which the participant is insured from Plan A for its cash surrender value. It is assumed for purposes of this revenue ruling

that Prohibited Transaction Exemption 92-6, 57 FR 5189 (February 12, 1992) applies to the purchase of a life insurance contract from Plan A and, thus, a participant's purchase of a life insurance contract from Plan A is not a prohibited transaction under § 4975. Employer M has nonhighly compensated employees that are not excludable employees within the meaning of § 1.410(b)-6, and the features of the life insurance contracts covering the lives of highly compensated employees are different than the features of the life insurance contracts covering the lives of nonhighly compensated employees. In addition, because of these differences in the features of the contracts, the rights that the nonhighly compensated employees have to purchase the life insurance contracts under which they are insured from Plan A are not of inherently equal or greater value than the rights that highly compensated employees have to purchase the life insurance contracts under which they are insured.

LAW AND ANALYSIS

Section 401(a)(4) provides that, under a qualified retirement plan, contributions or benefits provided under the plan must not discriminate in favor of highly compensated employees. Section 410(b) provides minimum coverage requirements that are designed to ensure that a qualified plan provides sufficient benefits to a large enough proportion of participants who are nonhighly compensated employees.

Section 1.401(a)(4)-1(b)(3) provides that a plan satisfies the requirements of § 401(a)(4) only if all benefits, rights and features provided under the plan are made available under the plan in a nondiscriminatory manner. Under § 1.401(a)(4)-4(a), benefits, rights and features (i.e., optional forms of benefit, ancillary benefits, and other rights or

features) are made available under the plan in a nondiscriminatory manner only if each benefit, right or feature satisfies the current availability requirement of § 1.401(a)(4)-4(b) and the effective availability requirement of § 1.401(a)(4)-4(c). In general, a benefit, right or feature satisfies the current availability requirement of § 1.401(a)(4)-4(b) for a plan year if the group of employees to whom the benefit, right or feature is currently available during the plan year satisfies § 410(b) (without regard to the average benefit percentage test of § 1.410(b)-5).

An other right or feature is any right or feature applicable to employees under the plan (other than a benefit formula, an optional form of benefit, or an ancillary benefit) that can be expected to have meaningful value. Under § 1.401(a)(4)-4(e)(3)(i), a distinct other right or feature exists if a right or feature is not available on substantially the same terms as another right or feature. Under § 1.401(a)(4)-4(e)(3)(iii)(C), the right to a particular form of investment, including, for example, a particular class or type of employer securities (taking into account, in determining whether different forms of investment exist, any differences in conversion, dividend, voting, liquidation preference, or other rights conferred under the security) is a distinct other right or feature. Similarly, differences in insurance contracts (e.g., differences in cash value growth terms or different exchange features) that may be purchased from a plan can create distinct other rights or features even if the terms under which the contracts are purchased from the plan are the same.

Under § 1.401(a)(4)-4(d)(4), an optional form of benefit, ancillary benefit, or other right or feature is permitted to be aggregated with another optional form of benefit, ancillary benefit, or other right or feature if one of the two is, in all cases, of inherently equal or

greater value than the other, and the optional form of benefit, ancillary benefit, or other right or feature that is of inherently equal or greater value separately satisfies the current availability requirement of § 1.401(a)(4)-4(b) and the effective availability requirement of § 1.401(a)(4)-4(c). For this purpose, one benefit, right, or feature is of inherently equal or greater value than another benefit, right, or feature only if, at any time and under any conditions, it is impossible for any employee to receive a smaller amount or a less valuable right under the first benefit, right, or feature than under the second benefit, right, or feature.

To the extent the purchase from Plan A of a life insurance contract by a highly compensated employee is a distribution alternative with respect to benefits described in § 411(d)(6)(A), such a purchase right is an optional form of benefit under Plan A. Even in situations in which this purchase right is not an optional form of benefit, this purchase right is an other right or feature. The purchase rights for the highly compensated employees are distinct optional forms of benefit or other rights or features from the purchase rights for nonhighly compensated employees because of differences in the life insurance contracts (analogous to a conversion right applicable to a security). This purchase right for highly compensated employees does not satisfy the current availability requirement of § 1.401(a)(4)-4(b) because the right to purchase the contracts of a type available to the highly compensated employees is not available to any nonhighly compensated employees, and therefore is not available to a group that satisfies the requirements of § 410(b). Moreover, under the facts presented, this purchase right of highly compensated employees cannot satisfy the requirements of § 1.401(a)(4)-4 through aggregation with any other optional form of benefit, ancillary benefit, or other right or feature (such as the purchase

right for nonhighly compensated employees) because no other optional form of benefit, ancillary benefit, or other right or feature under the plan that would enable the aggregated benefits to be available to a group that satisfies the requirements of § 410(b) is of inherently equal or greater value. Thus, Plan A fails to satisfy the nondiscrimination requirements of § 401(a)(4).

HOLDING

A plan that is funded, in whole or in part, with life insurance contracts does not satisfy the requirements of § 401(a)(4) prohibiting discrimination in favor of highly compensated employees where: (1) the plan permits highly compensated employees, prior to distribution of retirement benefits, to purchase those life insurance contracts prior to distribution; and (2) any rights under the plan for nonhighly compensated employees to purchase life insurance contracts from the plan prior to distribution of retirement benefits are not of inherently equal or greater value than the purchase rights of highly compensated employees.

DRAFTING INFORMATION

The principal authors of this revenue ruling are Larry Isaacs of Employee Plans, Tax Exempt and Government Entities Division, and Linda Marshall of the Office of the Division Counsel/Associate Chief Counsel, Tax Exempt and Government Entities. For further information regarding this revenue ruling, contact the Employee Plans taxpayer assistance telephone service between the hours of 8:00 a.m. and 6:30 p.m. Eastern Time, Monday through Friday, by calling (877) 829-5500 (a toll-free number). Mr. Isaacs may be reached

at (202) 283-9710, and Ms. Marshall may be reached at (202) 622-6090 (not toll-free numbers).

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.201: Rulings and determination letters.

(Also, Part I, §402; §1.402(a)-1.)

Rev. Proc. 2004-16

SECTION 1. PURPOSE

This revenue procedure is issued in connection with the issuance of proposed regulations under § 402(a) of the Internal Revenue Code regarding the valuation of life insurance contracts upon distribution from a qualified retirement plan and proposed regulations under §§ 79 and 83 regarding the valuation of life insurance contracts under those sections (REG-126967-03). The preamble to the proposed regulations states that it is not appropriate in some cases to use either the net surrender value of a distributed life insurance contract (i.e., the contract's cash value after reduction for any surrender charges) or the contract's reserves as the contract's fair market value upon distribution of an insurance contract from a qualified plan but the preamble provides limited guidance as to what value may be used instead. Similarly, the proposed regulations under §§ 79 and 83 clarify that the amount includible in income under those sections is based upon the fair market value of the insurance contract rather than its cash value but these proposed regulations do not provide any guidance as what constitutes fair market value. The regulations are generally proposed to apply beginning on the date the proposed regulations are filed in the Federal Register. The preamble to the proposed regulations also requests public comments regarding appropriate methods for valuing life insurance contracts when distributed from qualified retirement plans and for purposes of §§ 79 and 83. Until further guidance is issued, this revenue procedure provides interim rules under which the cash value (without reduction for surrender charges) of a life insurance contract may be treated as the contract's fair market value when the contract is distributed from a qualified plan under § 402 and for purposes of §§ 79 and 83.

SECTION 2. BACKGROUND

.01 Section 402(a) provides generally that any amount actually distributed to any distributee by any employees' trust described in § 401(a) which is exempt from tax under § 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under § 72.

.02 Section 1.402(a)-1(a)(*1*)(iii) of the current regulations provides, in general, that a distribution of property by a § 401(a) plan shall be taken into account by the distributee at its "fair market value." Section 1.402(a)-1(a)(*2*) of the current regulations provides, in general, that upon distribution of an annuity or life insurance contract, the "entire cash value" must be included in the distributee's income. The current regulations do not define "fair market value" or "entire cash value" and questions have arisen regarding the interaction between these two provisions.

.03 The proposed regulations would clarify that the requirement that a distribution of property must be included in the distributee's income at fair market value is controlling in those situations where the existing regulations provide for the inclusion of the entire cash value. Thus, the proposed regulations provide that, in those cases where a qualified plan distributes a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, the fair market value of such a contract is generally included in the distributee's income rather than the entire cash value of the contract. For this purpose, the policy cash value and all other rights under the contract (including any supplemental agreements thereto and whether or not guaranteed) are included in determining the fair market value of such a contract. The proposed regulations provide a similar rule for purposes of the valuation of such contracts under §§ 79 and 83.

.04 In Rev. Rul. 59-195, 1959-1 C.B. 18, the Service ruled that in situations similar to those where an employer purchases and pays the premiums on an insurance policy on the life of one of its employees and subsequently sells such policy, on which further premiums must be paid, the value of such policy, for computing taxable gain in the year of purchase, should be determined under the method of valuation prescribed in §25.2512-6 of the Gift Tax Regulations. Under this method, the value of such a policy is

not its cash surrender value but the interpolated terminal reserve at the date of sale plus the proportionate part of any premium paid by the employer prior to the date of the sale which is applicable to a period subsequent to the date of the sale. Section 25.2512-6 also provides that if "because of the unusual nature of the contract such approximation is not reasonably close to the full value, this method may not be used." Thus, this method may not be used to determine the fair market value of an insurance policy where the reserve does not reflect the value of all of the relevant features of the policy.

.05 In Q&A-10 of Notice 89-25, 1989-1 C.B. 662, the IRS addressed the question of what amount is includible in income under § 402(a) when a participant receives a distribution from a qualified plan that includes a life insurance policy with a value substantially higher than the cash surrender value stated in the policy. The notice noted the practice of using cash surrender value as fair market value for these purposes and concluded that this practice is not appropriate where the total policy reserves, including life insurance reserves (if any) computed under § 807(d), together with any reserves for advance premiums, dividend accumulations, etc., represent a much more accurate approximation of the policy's fair market value.

.06 Since Notice 89-25 was issued, life insurance contracts have been marketed that are structured in a manner which results in a temporary period during which neither a contract's reserves nor its cash surrender value represent the fair market value of the contract. For example, some life insurance contracts may provide for large surrender charges and other charges that are not expected to be paid because they are expected to be eliminated or reversed in the future (under the contract or under another contract for which the first contract is exchanged), but this future elimination or reversal is not always reflected in the calculation of the contract's reserve. If such a contract is distributed prior to the elimination or reversal of those charges, both the cash surrender value and the reserve under the contract could significantly understate the fair market value of the contract. Thus, the preamble to the proposed regulations states that, in some cases, it would not be appropriate to use either the net surrender value (i.e. the contract's cash value after reduction for any surrender charges) or, because of the unusual nature of the contract, the contract's reserves to determine the fair market value of the contract. Accordingly, Q&A-10 of Notice 89-25 should not be interpreted to

provide that a contract's reserves (including life insurance reserves (if any) computed under § 807(d), together with any reserves for advance premiums, dividend accumulations, etc.) are always an accurate representation of the contract's fair market value.

.07 As stated in the preamble to the proposed regulations, the amount of any distribution determined under § 402 also applies for purposes of determining the qualified status of any plan. For example, the fair market value of a distributed life insurance contract, determined in accordance with the proposed regulations and this revenue procedure, must be considered in determining whether the insured participant has received benefits in excess of the limits imposed by § 415.

.08 Section 79 generally requires that the cost of group-term life insurance coverage on the life of an employee that is in excess of $50,000 of coverage be included in the income of the employee. Pursuant to § 1.79-1(b) of the Income Tax Regulations, under specified circumstances group-term life insurance may be combined with other benefits, referred to as permanent benefits.

.09 Permanent benefits provided to an employee are subject to taxation under rules described in § 1.79-1(d). Under those rules, the cost of the permanent benefits, reduced by the amount paid for those benefits by the employee, is included in the employee's income. The cost of the benefits can be no less than an amount determined under a formula provided in the regulations. The formula is based in part on the increase in the employee's deemed death benefit during the year. One of the factors used for determining the deemed death benefit is "the net level premium reserve at the end of that policy year for all benefits provided to the employee by the policy or, if greater, the cash value of the policy at the end of that policy year."

.10 The proposed regulations would amend § 1.79-1(d) to delete the term cash value from the formula for determining the cost of permanent benefits and substitute the term fair market value. The purpose of the change is to clarify that, unless specifically excepted from the definition of permanent benefits, the value of all features of a life insurance policy providing an economic benefit to an employee (including, for example, the value of a springing cash value feature) must be included in the employee's income.

.11 Section 83(a) provides that when property is transferred to any person in connection with the performance of services, the service provider must include in gross income (as compensation income) the excess of the fair market value of the property, determined without regard to lapse restrictions (such as life insurance contract surrender charges), and determined at the first time that the transferee's rights in the property are either transferable or not subject to a substantial risk of forfeiture (i.e., when those rights become "substantially vested"), over the amount (if any) paid for the property. Section 1.83-3(e) provides that in the case of a transfer of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, only the cash surrender value of the contract is considered to be property. The proposed regulations generally would amend § 1.83-3(e) to provide that in the case of a transfer of an insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, the policy cash value and all other rights under the contract (including any supplemental agreements, whether or not guaranteed), other than current insurance protection, are treated as property for purposes of this section. However, in the case of the transfer of a life insurance contract, retirement income contract, endowment contract, or other contract providing life insurance protection, which was part of a split-dollar arrangement (as defined in § 1.61-22(j)) entered into on or before September 17, 2003, and which is not materially modified (as defined in § 1.61-22(j)(2)) after September 17, 2003, only the cash surrender value of the contract is considered to be property.

SECTION 3. INTERIM GUIDANCE FOR DETERMINING FAIR MARKET VALUE

.01 The Service and the Treasury recognize that many taxpayers could have difficulty determining the fair market value of an insurance contract after the issuance of the proposed regulations under §§ 79 and 83 and the clarification in the preamble to the proposed regulations under § 402 that Notice 89-25 should not be interpreted to provide that a contract's reserves (including life insurance reserves (if any) computed under § 807(d), together with any reserves for advance premiums, dividend accumulations, etc.) are always an accurate representation of the contract's fair market value. Accordingly, in connection with the proposed regulations, this revenue procedure

provides interim rules under which the cash value (without reduction for surrender charges) of a life insurance contract distributed from a qualified plan may be treated as the fair market value of that contract. These interim rules also apply for purposes of determining the value of insurance contracts under §§ 79 and 83.

.02 Cash value (without reduction for surrender charges) may be treated as the fair market value of a contract as of a determination date provided such cash value is at least as large as the aggregate of: (1) the premiums paid from the date of issue through the date of determination, plus (2) any amounts credited (or otherwise made available) to the policyholder with respect to those premiums, including interest, dividends, and similar income items (whether under the contract or otherwise), minus (3) reasonable mortality charges and reasonable charges (other than mortality charges), but only if those charges are actually charged on or before the date of determination and are expected to be paid.

.03 In those cases where the contract is a variable contract (as defined in § 817(d)) cash value (without reduction for surrender charges) may be treated as the fair market value of the contract provided such cash value is at least as large as the aggregate of: (1) the premiums paid from the date of issue through the date of determination, plus (2) all adjustments made with respect to those premiums during that period (whether under the contract or otherwise) that reflect investment return and the current market value of segregated asset accounts, minus (3) reasonable mortality charges and reasonable charges (other than mortality charges), but only if those charges are actually charged on or before the date of determination and are expected to be paid.

.04 The date of determination in the case of a distribution of a contract from a qualified plan is the date of that distribution. The date of determination in the case of the provision of permanent benefits subject to § 79 is the date those benefits are provided. The date of determination in the case of a transfer of an insurance contract subject to § 83 is the date on which fair market value must be determined under the rules of § 83.

SECTION 4. EFFECTIVE DATE

This revenue procedure is effective on February 13, 2004.

DRAFTING INFORMATION

The principal authors of this revenue procedure are Robert Walsh and Larry Isaacs of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue procedure as it pertains to § 402, please contact the Employee Plans' taxpayer assistance telephone service at 1-877-829-5500 (a toll-free number) between the hours of 8:00 a.m. and 6:30 p.m. Eastern Time, Monday through Friday. For further information regarding this revenue procedure as it pertains to § 79, please contact Betty Clary of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities) at (202) 622-6080 (not a toll-free number). For further information regarding this revenue procedure as it pertains to § 83, please contact Robert Misner of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities) at (202) 622-6030 (not a toll-free number). Mr. Walsh and Mr. Isaacs may be reached at (202) 283-9888 (not a toll-free number).

FROM THE OFFICE OF PUBLIC AFFAIRS

February 13, 2004
JS-1173

Department of the Treasury
Second Quarterly Update of the 2003 - 2004 Priority Guidance Plan
Joint Statement by:

Pamela F. Olson
Assistant Secretary (Tax Policy)
U.S. Department of the Treasury
Mark W. Everson
Commissioner
Internal Revenue Service
Emily A. Parker
Acting Chief Counsel
Internal Revenue Service

We are pleased to announce the second quarterly update of the 2003 - 2004 Priority Guidance Plan.

On July 24, 2003, we released the 2003 - 2004 Priority Guidance Plan listing 268 projects for the plan year beginning July 1, 2003 and ending June 30, 2004. In our Joint Statement that accompanied the release of the 2003 2004 Priority Guidance Plan, we emphasized our commitment to increased and more timely published guidance. We indicated that we would update the plan quarterly to reflect additional guidance that we intend to publish during the plan year. Updating the plan also provides flexibility to respond to developments arising during the year.

The attached update sets forth the guidance on the original 2003 - 2004 Priority Guidance Plan that we have published. Although the update may indicate that a particular item on the plan has been completed, it is possible that one or more additional projects may be completed in the plan year relating to that item. The update also includes 34 items of additional guidance, some of which have already been published.

We continue to invite the public to provide us with comments and suggestions as we identify and write guidance throughout the plan year.

The updated 2003 -2004 Priority Guidance Plan will be republished on the IRS website on the Internet (www.irs.gov) under Tax Professionals, IRS Resources, Administrative Information and Resources, 2003 2004 Priority Guidance Plan. Copies can also be obtained by calling Treasury's Office of Public Affairs at (202) 622-2960.

OFFICE OF TAX POLICY
AND
INTERNAL REVENUE SERVICE

2003-2004 PRIORITY GUIDANCE PLAN

FEBRUARY 13, 2004 UPDATE

CONSOLIDATED RETURNS

Original PGP Projects:

1. Guidance under section 1502 regarding transactions involving obligations of consolidated group members.

2. Guidance under section 1502 regarding rate or discount subsidy payments.

3. Final regulations under section 1502 regarding certain group structure changes.

4. Guidance under section 1502 regarding treatment of member stock.

Additional PGP Projects:

5. Guidance under section 1504(a)(5)(C) and (D) regarding affiliation.

6. Guidance under section 1502 regarding application of section 108 to members of a consolidated group.
- PUBLISHED 9/4/2003 in FR as TEMP 9089
- PUBLISHED 12/11/2003 in FR as TEMP 9098

CORPORATIONS AND THEIR SHAREHOLDERS

Original PGP Projects:

1. Final regulations regarding the effect of reorganizations on attribute reduction in respect of cancellation of indebtedness.

2. Guidance regarding redemptions of corporate stock.

3. Guidance regarding transactions involving the transfer or receipt of no net equity value.

4. Final regulations regarding taxable asset acquisitions and dispositions of insurance companies.

5. Guidance regarding the acquisition of businesses having certain nonqualified settlement funds.

6. Guidance regarding the effect of pre-closing changes of acquiror stock value on continuity of interest.

7. Guidance regarding the business purpose requirement under section 355.
   - PUBLISHED 11/17/2003 in IRB 2003-46 as REV. RUL. 2003-110 (released 10/23/2003)

8. Guidance regarding the active trade or business requirement under section 355(b).

9. Guidance regarding predecessors and successors under section 355(e).

10. Guidance regarding the assumption of liabilities in certain transfers of property.

11. Guidance regarding transfers of assets after putative reorganizations.

12. Guidance regarding certain cross-chain transactions.

13. Guidance under section 368(a)(1)(F).

14. Guidance under section 382.
    - PUBLISHED 10/6/2003 in IRB 2003-40 as NOTICE 2003-65 (released 9/12/2003)

15. Guidance under section 1374 regarding liquidations of C corporations.

EMPLOYEE BENEFITS

A. Retirement Benefits

Original PGP Projects:

1. Guidance on phased retirement arrangements.

2. Guidance on distribution rules for rollover contributions.
   - WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV RUL. 2004-12 (released 1/29/2004)

3. Guidance updating Rev. Rul. 81-100.

4. Proposed regulations under section 401(a)(4) for cash balance plans.

5. Regulations under section 401(a)(9) on required minimum distributions.

6. Guidance on whether employees of a section 501(c)(3) organization who are eligible to participate in a section 403(b) plan are excludable employees for section 401(k) and (m) plans.

7. Guidance relating to annuity plans under section 403(b).

8. Final regulations under section 408(q).

9. Guidance under section 409(p) on S corporation ESOPs.
   - PUBLISHED 2/9/2004 in IRB 2004-6 as REV. RUL. 2004-4 (released 1/23/2004)

10. Revenue ruling under section 410(b)(6)(c).
    - WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV. RUL. 2004-11 (released 1/29/2004)

11. Guidance under section 411(a).
    - WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV. RUL. 2004-10 (released 1/29/2004)

12. Guidance under sections 411(b)(1)(H) and 411(b)(2).

13. Guidance under section 411(d)(6).

14. Guidance on mortality tables.
    - PUBLISHED 9/22/2003 in IRB 2003-38 as NOTICE 2003-62 (released 9/3/2003)

15. Guidance on section 412(i) plans.
    - WILL BE PUBLISHED 2/17/2004 in FR as NPRM REG-126967-03

16. Additional transitional rules when a PEO retirement plan is converted to a multiple employer plan.

- PUBLISHED 12/15/2003 in IRB 2003-50 as REV. PROC. 2003-86 (released 11/25/2003)

17. Regulations under section 415.

18. Guidance on section 416(g)(4)(H) for safe harbor 401(k) plans.
- WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV. RUL. 2004-13 (released 1/29/2004)

19. Guidance on use of electronic technologies for various retirement plan transactions.
- PUBLISHED 2/9/2004 in IRB 2004-6 as NOTICE 2004-10 (released 1/20/2004)

20. Final regulations under section 417(a).
- PUBLISHED 12/17/2003 in FR as TD 9099

21. Guidance under section 417(e).

22. Guidance under section 420.

23. Guidance under section 457

24. Revenue Procedure on model provisions for section 457(b) plans.

25. Guidance under section 3405 on actions by a duly authorized agent.

Additional PGP Projects:

26. Notice on abusive Roth IRA transactions.
- PUBLISHED 1/26/2004 in IRB 2004-4 as NOTICE 2004-8 (released 12/31/2003)

27. Revenue procedure on funding waivers under section 412(d).
- WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV PROC. 2004-15 (released 1/29/2004)

28. Revenue ruling on nondiscrimination requirements for qualified plans selling life insurance to participants.
- WILL BE PUBLISHED 3/8/2004 in IRB 2004-10 as REV. RUL. 2004-21 (released 2/13/2004)

29. Revenue ruling on deduction limits for qualified plans holding life insurance.
- WILL BE PUBLISHED 3/8/2004 in IRB 2004-10 as REV. RUL. 2004-20 (released 2/13/2004)

30. Revenue procedure on determining fair market value of life insurance distributed from qualified plans or taxable under section 79 or section 83.
- WILL BE PUBLISHED 3/8/2004 in IRB 2004-10 as REV PROC. 2004-16 (released 2/13/2004)

B. Executive Compensation, Health Care and Other Benefits, and Employment Taxes

Original PGP Projects:

1. Guidance under section 35 on credit for health care insurance costs of eligible individuals.
- WILL BE PUBLISHED 3/1/2004 in IRB 2004-9 as REV. PROC. 2004-12 (released 2/12/2004)

2. Guidance on election between taxable and nontaxable benefits.

3. Guidance under section 62(c) on payments to couriers.
- PUBLISHED 1/26/2004 in IRB 2004-4 as REV. RUL. 2004-1 (released 1/15/2004)

4. Revenue ruling on electronic receipts and accountable plans.
- PUBLISHED 11/3/2003 in IRB 2003-44 as REV. RUL. 2003-106 (released 10/20/2003)

5. Guidance under section 83.

6. Guidance on disability payments.

7. Guidance on HRAs.

8. Revenue ruling under section 105 on nonprescription drugs.
- PUBLISHED 9/22/2003 in IRB 2003-38 as REV. RUL. 2003-102 (released 9/3/2003)

9. Guidance on debit cards.

10. Revenue ruling on the application of section 280G to various bankruptcy situations.

11. Guidance on health care provider incentive payments.

12. Final regulations on Incentive Stock Options.

13. Guidance on the employment taxation and reporting requirements applicable to interest in nonstatutory stock options and deferred compensation transferred to a former spouse incident to divorce.

14. Guidance under section 3121 regarding the definition of salary reduction agreement.

15. Guidance on the employment tax treatment of bonuses paid to employees on the signing of a collectively bargained agreement.

16. Guidance on FICA and FUTA tax with respect to incentive stock options under section 422 and employee stock purchase plans under section 423.

17 Notice on issues with respect to the treatment of choreworkers.
- PUBLISHED 10/27/2003 in IRB 2003-43 as NOTICE 2003-70 (released 10/3/2003)

18. Guidance on the reporting procedures for successor organizations following Rev. Proc. 96-60.

19. Guidance under section 3504.

20. Revenue ruling under section 4980B on Medicare entitlement as a second qualifying event.
- WILL BE PUBLISHED 3/8/2004 in IRB 2004-10 as REV. RUL. 2004-22 (released 2/13/2004)

21. Guidance on tips paid to restaurant employees.

22. Guidance on the deposit requirements for employment tax in connection with

the exercise of nonstatutory options.

Additional PGP Projects:

23. Notice on health savings accounts.
- PUBLISHED 1/12/2004 in IRB 2004-2 as NOTICE 2004-2 (released 12/22/2003)

24. Guidance on the tax treatment of payments under the Smallpox Emergency Personnel Protection Act.

25. Additional guidance on health savings accounts.

EXCISE TAXES

Original PGP Projects:

1. Final regulations under section 4051 regarding the definition of highway vehicle in sections 145.4051 and 48.4061(a)-1.

2. Guidance regarding the definition of highway tractors subject to the heavy truck tax under section 4051.

3. Guidance under section 4051(a)(2) and (3) regarding suitability for use.

4. Guidance under section 4081 regarding the entry into the United States of taxable fuel.

5. Final regulations under section 4252 regarding toll telephone services.

6. Guidance under section 4261 regarding resellers of air transportation.

7. Guidance under section 4291 regarding the duties of the collector of collected excise taxes.

8. Proposed regulations under section 6416(a)(4) regarding claims for gasoline tax.

EXEMPT ORGANIZATIONS

Original PGP Projects:

1. Guidance on joint ventures between exempt organizations and for-profit companies.

2. Guidance on low-income housing partnerships and 501(c)(3) participation.

3. Guidance on downpayment assistance organizations.

4. Guidance on section 501(c)(4) organizations.
- PUBLISHED 1/26/2004 in IRB 2004-4 as REV. RUL. 2004-6 (released 12/23/2003)

5. Guidance concerning the internet and unrelated business income tax.

6. Regulations under section 529 regarding qualified tuition programs.

7. Guidance on reporting requirements applicable to Coverdell education savings

accounts.

- PUBLISHED 8/18/2003 in IRB 2003-33 as NOTICE 2003-53 (released 7/31/2003)

8. Guidance on split interest trusts.

Additional PGP Projects:

9. Announcement on suspension of tax exempt status.

- PUBLISHED 12/1/2003 in IRB 2003-48 as ANN. 2003-74 (released 11/14/2003)

FINANCIAL INSTITUTIONS AND PRODUCTS

Original PGP Projects:

1. Proposed regulations regarding accruals on sales of REMIC regular interests between payment dates.

2. Guidance on system upgrade payments made to utilities.

3. Final regulations under section 263(g).

4. Guidance under section 265(a)(2).

5. Proposed regulations on notional principal contracts.

6. Revenue ruling under section 446 concerning the timing rules of hedging transactions not identified under section 1.1221-2(f).

- PUBLISHED 12/29/2003 in IRB 2003-52 as REV. RUL. 2003-127

7. Final regulations addressing the treatment of inducement fees for REMIC residual interests.

8. Proposed regulations addressing valuation under section 475.

9. Final regulations under section 475(e) and (f).

10. Guidance under section 851 on the treatment of certain obligations backed by Treasury securities for RIC diversification purposes.

11. Revenue ruling under section 856 on customary services performed by REITs.

- WILL BE PUBLISHED 3/8/2004 in IRB 2004-10 as REV. RUL. 2004-24

12. Advance notice of proposed rulemaking on interest-only REMIC regular interests.

13. Final regulations on REMIC residual interests.

14. Guidance on credit card transactions.

15. Guidance under section 7872.

Additional PGP Projects:

16. Proposed regulations clarifying the application of the TEFRA audit procedures to REMICs.

17. Guidance regarding the application of section 1(h) to capital gain dividends of RICs and REITs.

18. Revenue ruling under sections 1233 and 1259 regarding the transfer of a short sale position from one broker to another.
- WILL BE PUBLISHED 2/23/2004 in IRB 2004-8 as REV. RUL. 2004-15 (released 1/28/2004)

19. Guidance on tax avoidance transactions using offsetting forward currency option contracts.
- PUBLISHED 12/22/2003 in IRB 2003-51 as NOTICE 2003-81

20. Guidance under section 853 regarding foreign tax credit reporting by regulated investment companies.

GENERAL TAX ISSUES

Original PGP Projects:

1. Proposed regulations under section 21 regarding the credit for household and dependent care expenses.

2. Final revenue procedure under section 23 regarding the credit for adoption expenses.

3. Guidance under section 32.

4. Guidance under section 41 regarding the research credit.
- PUBLISHED 1/2/2004 in FR as TD 9104
- PUBLISHED 1/2/2004 in FR as ANPRM REG-153656-03

5. Final regulations under section 41 regarding the computation of the research credit in a controlled group.

6. Guidance under section 42.
- PUBLISHED 11/24/2004 in IRB 2003-47 as REV. PROC. 2003-82

7. Final regulations under sections 1.42-6 and 1.42-14 to conform to statutory changes.
- PUBLISHED 1/6/2004 in FR as TD 9110

8. Guidance under section 45D regarding the new markets tax credit.
- PUBLISHED 8/25/2003 in IRB 2003-34 as NOTICE 2003-56 (released 7/22/2003)
- PUBLISHED 9/29/2003 in IRB 2003-39 as NOTICE 2003-64 (released 9/5/2003)
- PUBLISHED 10/14/2003 in IRB 2003-41 as NOTICE 2003-68 (released 9/23/2003)

9. Final regulations under sections 46 and 167 relating to normalization.

10. Guidance under sections 51 and 51A on qualified IV-A recipient.
- PUBLISHED 11/10/2003 in IRB 2003-45 as REV. RUL. 2003-112 (released 10/17/2003)

11. Guidance regarding the section 59(e) election.

12. Revenue ruling regarding disaster relief payments to businesses.

13. Revenue ruling under sections 61 and 162 on the proper treatment of Medicaid rebates paid by pharmaceutical companies.

14. Guidance regarding the treatment of employee relocation costs.

15. Final regulations under section 121(c) regarding the reduced maximum exclusion for gain on the sale of a principal residence.

16. Revenue ruling under sections 121 and 1031 regarding like-kind exchange of a principal residence.

17. Guidance under section 152 regarding the release of a claim for exemption for a child of divorced or separated parents.

18. Guidance under section 165 regarding the deduction for worthless stock of subsidiaries for which an election under the check-the-box regulations has been made.
- PUBLISHED 12/24/2003 in IRB 2003-52 as REV. RUL. 2003-125

19. Final regulations under section 167 regarding the income forecast method.

20. Proposed and temporary regulations under section 168 relating to like-kind exchanges.

21. Final regulations under section 168 regarding depreciation of property for which the use changes.

22. Proposed and temporary regulations under sections 168 and 1400L regarding special depreciation allowance.
  - PUBLISHED 9/8/2003 in FR as TEMP 9091

23. Guidance under section 168 regarding changes in classification of property.
- PUBLISHED 1/2/2004 in FR as TEMP 9105

24. Guidance under section 168 on asset classes and activity classes under Rev. Proc. 87-56.

25. Guidance under section 172 regarding specified liability losses.

26. Guidance under section 174 regarding the treatment of inventory property.

27. Guidance under section 179 on elections.

28. Final regulations under section 221 regarding interest on education loans.

29. Revenue procedure under section 274 regarding the use of statistical sampling.

30. Final regulations under section 280F regarding vans and light trucks.

31. Final regulations under section 465 regarding interest other than as a creditor.

32. Guidance under section 1031 regarding reverse like-kind exchanges of property.

33. Revenue ruling under section 1241 on cancellation of lease or distributor agreements.

34. Guidance on corporations chartered under Indian tribal law.

Additional PGP Projects:

35. Revenue ruling under sections 61, 104, 130, and 139 regarding payments made
to claimants of the September 11th Victim Compensation Fund of 2001.
- PUBLISHED 11/17/2003 in IRB 2003-46 as REV. RUL. 2003-115

36. Notice regarding charitable contributions of patents and other intellectual property.
- PUBLISHED 1/20/2004 in IRB 2004-3 as NOTICE 2004-7

37. Guidance under section 1031 regarding the use of SIC codes in like kind exchanges of depreciable tangible property.

38. Notice under section 29 regarding chemical change.
- PUBLISHED 11/17/2003 in IRB 2003-46 as NOTICE 2003-70 (released 10/29/2003)

39. Final regulations under section 42 removing a barrier to the electronic filing of Form 8609 relating to the low-income housing credit.
- PUBLISHED 1/27/2004 in FR as TD 9112

40. Revenue procedure under section 446 regarding improper to proper depreciation changes.
- PUBLISHED 1/20/2004 in IRB 2004-3 as REV. PROC. 2004-11 (released 12/30/2003)

GIFTS, ESTATES AND TRUSTS

Original PGP Projects:

1. Guidance under section 642(c) regarding the contribution of a qualified conservation easement.
- PUBLISHED 12/15/2003 in IRB 2003-50 as REV RUL. 2003-123

2. Final regulations under section 643 regarding state law definition of income for trust purposes.
- PUBLISHED 1/2/2004 in FR as TD 9102

3. Update revenue procedures under section 664 containing sample charitable remainder unitrust provisions.

4. Guidance under section 664 regarding dividends and capital gains for charitable remainder trusts.
- PUBLISHED 11/20/2003 in FR as NPRM REG-110896-98

5. Final regulations under section 671 regarding reporting requirements for widely-held fixed investment trusts.

6. Guidance under sections 671 and 2036 regarding tax reimbursement provisions in grantor trusts.

7. Guidance under section 2032 regarding section 301.9100 relief.
- PUBLISHED 12/24/2003 in FR as NPRM REG-139845-02

8. Guidance under section 2053 regarding post-death events.

9. Guidance under section 2632 regarding the election out of the deemed allocation of the generation-skipping transfer tax exemption.

10. Guidance under section 2642 regarding issues related to the generation-skipping transfer tax exemption.

11. Guidance under section 2642 regarding qualified severance.

12. Guidance under section 2651 regarding the predeceased parent rule.

13. Guidance under section 2704 regarding the liquidation of an interest.

Additional PGP Projects:

14. Guidance under section 2702 regarding qualified interests.
    - PUBLISHED 11/3/2003 in IRB 2003-44 as NOTICE 2003-72 (released 10/15/2003)

15. Revenue ruling under section 642(c) regarding governing instrument requirements.
    - PUBLISHED 1/20/2004 in IRB 2004-3 as REV. RUL. 2004-5

INSURANCE COMPANIES AND PRODUCTS

Original PGP Projects:

1. Revenue ruling concerning reserves used to calculate required interest under section 812.
    - PUBLISHED 12/1/2003 in IRB 2003-48 as REV. RUL. 2003-120

2. Guidance regarding substantially equal periodic payments under section 72(q).
    - WILL BE PUBLISHED 3/1/2004 in IRB 2004-9 as NOTICE 2004-15

3. Guidance regarding the 2001 CSO mortality tables.

4. Guidance regarding split-dollar life insurance.
    - PUBLISHED 9/17/2003 in FR as TD 9092

Additional PGP Projects:

5. Revenue ruling describing prior guidance on split-dollar life insurance that, due to subsequent guidance, is obsolete.
    - PUBLISHED 10/6/2003 in IRB 2003-40 as REV. RUL. 2003-105

6. Final regulations under section 817

INTERNATIONAL ISSUES

A. Subpart F/Deferral

Original PGP Projects:

1. Regulations on the allocation of subpart F income.

2. Regulations under section 959 on previously taxed earnings and profits.

3. Guidance on the PFIC provisions.

B. Inbound Transactions

Original PGP Projects:

1. Guidance on cross-border pension distributions.

2. Guidance under section 1441.

3. Guidance on securities lending.

4. Guidance on the treatment of certain financial products for withholding purposes.

5. Regulations under section 1446.

6. Regulations relating to the reporting of bank deposit interest.

C. Outbound Transactions

Original PGP Projects:

1. Guidance on international restructurings.

2. Guidance follow-up to Notice 2003-46.
   - PUBLISHED 10/22/2003 in FR as TD 9093 and NPRM REG-110385-99

D. Foreign Tax Credits

Original PGP Projects:

1. Regulations on the allocation of foreign taxes under section 901.

2. Regulations under sections 902 and 904.

3. Regulations on look-through treatment for 10/50 company dividends (see Notice 2003-5).

4. Regulations on the change of taxable year and foreign tax credits.

E. Transfer Pricing

Original PGP Projects:

1. Regulations on the treatment of cross-border services.

2. Regulations on cost sharing under section 482.

3. Guidance on the APA process (Rev. Proc. 96-53).

4. Regulations on global dealing.

F. Sourcing and Expense Allocation

Original PGP Projects:

1. Guidance on interest expense apportionment.

2. Regulations on the allocation and apportionment of charitable contributions.

3. Regulations relating to the treatment of fringe benefits.

4. Guidance on the source of payments for cross-border use of property.

5. Regulations under sections 863(d) and (e).

G. Treaties

Original PGP Projects:

1. Treaty guidance on the determination of residence for dual resident companies.

2. Treaty guidance under the independent services article for nonresident partners.
- WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV. RUL. 2004-3 (released 1/29/2004)

3. Guidance on the procedures for claiming treaty waiver of insurance excise tax.
- PUBLISHED 11/10/2003 in IRB 2003-45 as REV. PROC. 2003-78 (released 10/10/2003)

4. Guidance on reporting for Canadian RRSPs and other plans.
- PUBLISHED 8/25/2003 in IRB 2003-34 as NOTICE 2003-57 (released 8/1/2003)
- PUBLISHED 12/8/2003 in IRB 2003-49 as NOTICE 2003-75 (released 11/26/2003)

H. Other

Original PGP Projects:

1. Guidance on the definition of "qualified foreign corporation" for purposes of taxation of dividends received by individuals.
- PUBLISHED 10/20/2003 in IRB 2003-42 as NOTICE 2003-69 (released 9/30/2003)
- PUBLISHED 10/27/2003 in IRB 2003-43 as NOTICE 2003-71 (released 10/3/2003)
- PUBLISHED 12/15/2003 in IRB 2003-50 as NOTICE 2003-79 (released 11/26/2003)

2. Regulations under section 269B.

3. Guidance on cross-border insurance issues.

4. Guidance on possessions issues.

5. Regulations concerning the treatment of currency gain or loss.

6. Regulations under section 1503(d).

Additional PGP Projects:

7 Revenue ruling relating to convention benefits under section 274(h).
- PUBLISHED 10/20/2003 in IRB 2003-42 as REV. RUL. 2003-109 (released 9/30/2003)

8. Announcement of agreement relating to the limitation on benefits article in the U.S.- Swiss Income Tax Convention.
- PUBLISHED 10/6/2003 in IRB 2003-40 as ANN. 2003-59

9. Announcement of agreement relating to deferred compensation under the U.S.- Austrian Income Tax Convention.

- PUBLISHED 10/6/2003 in IRB 2003-40 as ANN. 2003-58

10. Announcement of agreement implementing the mutual agreement procedures of the U.S.-Dutch Income Tax Convention.
    - PUBLISHED 11/10/2003 in IRB 2003-45 as ANN. 2003-63

11. Notice regarding information reporting with respect to foreign disregarded entities.
- PUBLISHED 1/26/2004 in IRB 2004-4 as NOTICE 2004-4 (released 12/29/2003)

12. Regulations regarding electronic filing of duplicate forms 5472.
- PUBLISHED 2/9/2004 in FR as TEMP 9113 and NPRM REG-167217-03

PARTNERSHIPS

Original PGP Projects:

1. Guidance regarding partnership transactions under section 337(d).

2. Final regulations under section 460 regarding partnership transactions for long-term contracts.

3. Final regulations under section 704(b) regarding capital account book-up.

4. Guidance under section 704(b) regarding the allocation of foreign tax credits.

5. Guidance under section 704(c).
- PUBLISHED 11/24/2003 in FR as NPRM REG-160330-02

6. Guidance under section 707 regarding disguised sales.

7. Proposed regulations under section 721 regarding partnership interests issued for services and the treatment of compensatory partnership options.

8. Update of the section 751 regulations.

9. Final regulations under section 752 regarding the assumption of partner liabilities.

10. Guidance under section 752 where a general partner is a disregarded entity.

11. Guidance on the application of section 1045 to certain partnership transactions.

12. Guidance under section 6031 on the reporting requirements of tax-exempt bond partnerships.
- PUBLISHED 11/10/2003 in FR as TEMP 9094
- PUBLISHED 12/1/2003 in IRB 2003-48 as REV. PROC. 2003-84 (released 11/6/2003)

13. Guidance under section 7701 regarding Delaware Statutory Trusts.

14. Guidance under section 7701 regarding disregarded entities and collection issues.

Additional PGP Projects:

15. Notice under section 772 regarding dividends as a separately stated item.

- WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as NOTICE 2004-5 (released 1/27/2004)

SUBCHAPTER S

Original PGP Projects:

1. Revenue ruling under section 1361 regarding QSub elections.

2. Guidance on the treatment of LIFO recapture under section 1363(d).

3. Guidance under section 7701 on deemed corporation entity elections for electing S corporations.

Additional PGP Projects:

4. Revenue procedure under section 1362 regarding S corporation rollover to IRA.
   - WILL BE PUBLISHED 2/17/2004 in IRB 2004-7 as REV. PROC. 2004-14

TAX ACCOUNTING

Original PGP Projects:

1. Final regulations under sections 162 and 263 regarding the deduction and capitalization of expenditures for intangible assets.
   - PUBLISHED 1/5/2004 in FR as TD 9107

2. Regulations under sections 162 and 263 regarding the deduction and capitalization of expenditures for tangible assets.
   - PUBLISHED 1/20/2004 in IRB 2004-3 as NOTICE 2004-6

3. Guidance under sections 162 and 263 regarding the deduction and capitalization of costs incurred to fertilize established timber stands.

4. Revenue ruling regarding the deduction and capitalization of costs incurred by utilities to maintain assets used to generate power.

5. Guidance under sections 165 regarding the treatment of preproduction costs of creative property.

6. Regulations under section 263A regarding the simplified service cost and simplified production methods.

7. Guidance under section 263A regarding “negative” additional section 263A costs.

8. Final regulations under sections 263A and 448 regarding adjustments under section 481(a) for certain changes in accounting method.

9. Regulations under section 381 regarding changes in method of accounting.

10. Guidance under section 442 regarding the period for taking into account adjustments resulting from certain changes in annual accounting period by pass-through entities.
    - PUBLISHED 11/10/2003 in IRB 2003-45 as REV. PROC. 2003-79

11. Revenue procedure under section 446 regarding changes in method of accounting for rotable spare parts.

12. Regulations under section 446 regarding methods of accounting.

13. Temporary regulations under section 448 regarding the nonaccrual experience method.
   - PUBLISHED 9/4/2003 in FR as TEMP 9090

14. Final revenue procedure under section 451 regarding the treatment of advance payments.

15. Revenue ruling under section 461 regarding the proper year for the deduction of payroll taxes on deferred compensation by accrual method taxpayers.

16. Regulations under section 468B regarding certain escrow funds.

17. Guidance on the tax treatment of vendor allowances involving buildouts and image upgrades.

18. Revenue ruling under section 1341 regarding the claim of right.
   - WILL BE PUBLISHED 2/23/2004 in IRB 2004-8 as REV. RUL. 2004-17 (released 2/6/2004)

Additional PGP Projects:

19. Notice under section 263A regarding the simplified service cost and simplified production methods.
   - PUBLISHED 9/2/2003 in IRB 2003-35 as NOTICE 2003-59

20. Revenue ruling under section 263A regarding the treatment of environmental remediation expenses.
   - WILL BE PUBLISHED 2/23/2004 in IRB 2004-8 as REV. RUL. 2004-18 (released 2/6/2004)

21. Final, temporary and proposed regulations under section 461(f) regarding transfers to satisfy contested liabilities.
   - PUBLISHED 11/21/2003 in FR as TD 9095 and NPRM REG-136890-02

22. Notice under section 461(f) identifying certain transfers to trusts for contested liabilities as listed transactions.
   - PUBLISHED 12/8/2003 in IRB 2003-49 as NOTICE 2003-77 (released 11/19/2003)

23. Guidance providing procedures under which taxpayers may obtain automatic consent to change a method of accounting to comply with sections 1.263(a)-4 and 1.263(a)-5.

24. Guidance regarding the treatment of capitalized costs in certain transactions involving the acquisition of a trade or business or a change in the capital structure of a business entity.

TAX ADMINISTRATION

Original PGP Projects:

1. Update Rev. Proc. 85-35 regarding claims for relief by victims of terrorism.

2. Final regulations under section 5891 regarding structured settlement factoring transactions.

3. Annual compilation of Tax Shelter Listed Transactions under section 6011.
   - PUBLISHED 12/8/2003 in IRB 2003-49 as NOTICE 2003-76

(released 11/7/2003)

4. Final regulations regarding electronic payee statements.

5. Proposed regulations regarding what constitutes a return under section 6020(b) for purposes of applying the failure to pay penalty.

6. Guidance regarding information reporting under section 6041 for commissions paid to insurance agents.

7. Revenue ruling regarding information reporting for royalty payments under sections 6041 and 6050N.

8. Final regulations regarding information reporting and backup withholding for purchasing card transactions.

9. Revenue procedure regarding Qualified Payment Card Agents.

10. Guidance regarding information reporting with respect to payments in lieu of dividends made to individuals.
- PUBLISHED 10/6/2003 in IRB 2003-40 as NOTICE 2003-67 (released 9/16/2003)
- PUBLISHED 12/29/2003 in FR as TD 9103

11. Final regulations under section 6045(f) regarding the reporting of gross proceeds to attorneys.

12. Final regulations under section 6050P regarding information reporting for cancellation of indebtedness.

13. Final regulations under section 6091 regarding hand carrying returns.

14. Proposed regulations under section 6103 regarding the disclosure of unrelated third party tax information in tax proceedings.

15. Final regulations under section 6103 regarding the definition of "agent"
- PUBLISHED 1/6/2004 in FR as TD 9111

16. Revenue procedure under section 6103 regarding fees charged for furnishing certain returns and return information.
- PUBLISHED 10/27/2003 in IRB 2003-43 as REV PROC. 2003-74

17. Final regulations regarding the ability of a return preparer to furnish a completed copy of an income tax return to the taxpayer using a medium other than paper.

18. Withdrawal of regulations under former section 6152 relating to the election by a decedent's estate to pay income tax in installments.
- PUBLISHED 12/3/2003 in FR as TD 9096

19. Update Rev. Ruls. 75-365, 366, and 367 regarding interests in real estate held by a decedent.

20. Guidance regarding the use of summary assessment procedures with respect to claimed Black Reparations and similar credits.

21. Guidance under section 6213 regarding math error assessments based on a Form W-2.

22. Revenue ruling regarding the classification of items and the statute of limitations under the TEFRA partnership provisions.

23. Revenue ruling under section 6231 regarding the application of certain TEFRA partnership provisions to disregarded entities.

24. Final regulations under section 6302 regarding the minimum threshold for depositing FUTA taxes.

25. Proposed regulations under sections 6320 and 6330 regarding collection due process.

26. Notice regarding collection issues relating to property held as a tenancy by the entirety arising from the Supreme Court's opinion in United States v. Craft.

- PUBLISHED 9/29/2003 in IRB 2003-39 as NOTICE 2003-60 (released 9/11/2003)

27. Revenue ruling regarding the limitations on setoff.

28. Revenue ruling regarding setoff with respect to a taxpayer in bankruptcy.

29. Proposed regulations under section 6655 regarding estimated tax payments by corporations.

30. Final regulations under sections 6662 and 6664 regarding penalties relating to tax shelters.

- PUBLISHED 12/30/2003 in FR as TD 9109

31. Revenue procedure regarding the submission and processing of offers-in-compromise.

- PUBLISHED 9/8/2003 in IRB 2003-36 as REV. PROC. 2003-71 (released 8/21/2003)

32. Final regulations imposing a user fee for offers-in-compromise.

- PUBLISHED 8/15/2003 in FR as TD 9086

33. Guidance necessary to facilitate electronic tax administration.

34. Final regulations under section 7430 regarding qualified offers.

- PUBLISHED 12/29/2003 in FR as TD 9106

35. Proposed regulations under section 7430 regarding miscellaneous changes made by TRA 97 and RRA 98.

36. Update Rev. Proc. 87-24 regarding docketed Tax Court cases.

37. Proposed regulations regarding third party and John Doe summonses.

38. Revenue procedure regarding the early examination of questionable transactions.

39. Revisions to Circular 230 regarding practice before the IRS.

- PUBLISHED 12/30/2003 in FR as NPRM REG-122379-02

40. Revenue procedure expanding the prefiling agreement program.

Additional PGP Projects:

41. Announcement regarding a delay of the implementation of the new rolling renewal schedule for enrolled agents to renew their enrollment under Circular 230.

- PUBLISHED 11/10/2003 in IRB 2003-45 as ANN. 2003-68 (released 10/27/2003)

42. Revenue ruling under section 6323 regarding the effect of actual knowledge of a tax lien for priority purposes.
- PUBLISHED 11/3/2003 in IRB 2003-44 as REV. RUL. 2003-108

43. Proposed regulations under section 6011 to remove impediments to electronic filing of certain business returns.
- PUBLISHED 12/19/2003 in FR as NPRM REG-116664-01

44. Notice under section 6001 establishing a pilot program for entering into a record keeping agreement relating to the research credit under section 41.
- PUBLISHED 2/9/2004 in IRB 2004-6 as NOTICE 2004-11

45. Revenue ruling under section 6402 regarding post-petition credits in chapter 13 bankruptcy cases.

46. Temporary regulations under sections 6043 and 6045 regarding information reporting relating to taxable stock transactions.
- PUBLISHED 12/30/2003 in FR as TEMP 9101
- PUBLISHED 1/26/2004 in IRB 2004-4 as NOTICE 2004-9 (released 12/30/2003)

47. Guidance under section 6041 regarding information reporting relating to debit or credit card payments of health expenses.
- WILL BE PUBLISHED 3/1/2004 in IRB 2004-9 as NOTICE 2004-16

48. Notice providing relief to health insurance providers from the section 6050T information reporting requirements.

49. Notice regarding changes to the ITIN application process.
- PUBLISHED 1/12/2004 in IRB 2004-2 as NOTICE 2004-1 (released 12/18/2003)

50. Revenue ruling under section 6402 regarding offset under the community property laws of various states.

51. Revenue ruling regarding the liability of multi-members of a limited liability company for employment taxes.

52. Notice regarding the use of signature stamps by practitioners.

53. Final regulations under section 6011 regarding confidential transactions.
- PUBLISHED 12/30/2003 in FR as TD 9108

TAX EXEMPT BONDS

Original PGP Projects:

1. Guidance under section 141 regarding naming rights.

2. Guidance on correction alternatives and voluntary compliance for tax exempt bond provisions.

3. Final regulations under section 141 on refundings.

4. Proposed regulations under section 141 regarding allocation and accounting provisions.

5. Regulations under section 142 regarding solid waste disposal facilities.

6. Guidance under section 143 regarding mortgage insurance fees.

- PUBLISHED 11/5/2003 in FR as NPRM REG-146692-03

7 Guidance under section 143 regarding average area purchase price.
- WILL BE PUBLISHED 3/1/2004 in IRB 2004-9 as REV. PROC. 2004-18 (released 2/10/2004)

8. Final regulations under section 148 regarding brokers' commissions and similar fees.
- PUBLISHED 12/11/2003 in FR as TD 9097

9. Guidance on arbitrage.

10. Guidance under section 150 regarding change in use provisions.

11. Guidance under section 1397E regarding qualified zone academy bonds.

Additional PGP Projects:

12. Revenue ruling under section 147(e) regarding helicopters.
- 11/17/2003 in IRB 2003-46 as REV. RUL. 2003-116 (released 10/29/2003)

APPENDIX - Regularly Scheduled Publications

JULY 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 7/7/2003 in IRB 2003-27 as REV. RUL. 2003-71

2. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in July 2003.
- PUBLISHED 7/28/2003 in IRB 2003-30 as NOTICE 2003-48 (released 7/3/2003)

3. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
- PUBLISHED 7/21//2003 in IRB 2003-29 as REV. RUL. 2003-87

AUGUST 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 8/18/2003 in IRB 2003-33 as REV. RUL. 2003-94

2. Revenue procedure providing the amounts of unused housing credit carryover allocated to qualified states under section 42(h)(3)(D) for the calendar year.
- PUBLISHED 8/25/2003 in IRB 2003-34 as REV. PROC. 2003-67

3. Notice providing the inflation adjustment factor to be used in determining the enhanced oil recovery credit under section 43 for tax years beginning in the calendar year.
- PUBLISHED 7/14/2003 in IRB 2003-28 as NOTICE 2003-43

4. Notice providing the applicable percentage to be used in determining percentage depleting for marginal properties under section 613A for the calendar year.

- PUBLISHED 7/29/2003 in IRB 2003-30 as NOTICE 2003-54

5. Revenue ruling setting forth the terminal charge and the standard industry fare level (SIFL) cents-per-mile rates for the second half of 2003 for use in valuing personal flights on employer-provided aircraft.
   - PUBLISHED 9/15/2003 in IRB 2003-37 as REV. RUL. 2003-89

6. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in August 2003.
   - PUBLISHED 9/2/2003 in IRB 2003-25 as NOTICE 2003-58 (released 8/6/2003)

7. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
   - PUBLISHED 8/25/2003 in IRB 2003-34 as REV. RUL. 2003-100

SEPTEMBER 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
   - PUBLISHED 9/8/2003 in IRB 2003-36 as REV. RUL. 2003-101

2. Revenue ruling providing the monthly bond factor amounts to be used by taxpayers who dispose of qualified low-income buildings or interests therein during the period July through September, 2003.
   - PUBLISHED 8/18/2003 in IRB 2003-33 as REV. RUL. 2003-93

3. Revenue ruling under section 6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period October through December 2003.
- PUBLISHED 9/29/2003 in IRB 2003-39 as REV. RUL. 2003-104

4. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in September 2003.
- PUBLISHED 9/22/2003 in IRB 2003-38 as NOTICE 2003-63 (released 9/4/2003)

5. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
- PUBLISHED 9/22/2003 in IRB 2003-38 as REV. RUL. 2003-103

6. Revenue procedure under section 62 regarding the deduction and deemed substantiation of federal standard mileage amounts.
   - PUBLISHED 10/27/2003 in IRB 2003-43 as REV. PROC. 2003-76

7. Revenue procedure under section 62 regarding the deduction and deemed substantiation of federal travel per diem amounts.
   - PUBLISHED 11/10/2003 in IRB 2003-45 as REV. PROC. 2003-80

8. Update Notice 2002-62 to add approved applicants for designated private delivery service status under section 7502(f). Will be published only if any new applicants are approved.
- CLOSED WITHOUT PUBLICATION

OCTOBER 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.

- PUBLISHED 10/14/2003 in IRB 2003-41 as REV. RUL. 2003-107 (released 9/17/2003)

2. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in October 2003.
- PUBLISHED 10/20/2003 in IRB 2003-42 as NOTICE 2003-61 (released 10/6/2003)

3. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
   - PUBLISHED 11/3/2003 in IRB 2003-44 as REV RUL. 2003-113

4. Revenue procedure under section 1 and other sections of the Code regarding the inflation adjusted items for 2004.
- PUBLISHED 12/8/2003 in IRB 2003-49 as REV. PROC. 2003-85

5. Revenue procedure providing the loss payment patterns and discount factors for the 2003 accident year to be used for computing unpaid losses under section 846.
- PUBLISHED 1/12/2004 in IRB 2004-2 as REV PROC. 2004-9 (released 12/17/2003)

6. Revenue procedure providing the salvage discount factors for the 2003 accident year to be used for computing discounted estimated salvage recoverable under section 832.
- PUBLISHED 1/12/2004 in IRB 2004-2 as REV. PROC. 2004-10 (released 12/17/2003)

7. Update of Rev. Proc. 2002-71 listing the tax deadlines that may be extended by the Commissioner under section 7508A in the event of a Presidentially-declared disaster or terrorist attack.
- PUBLISHED 1/26/2004 in IRB 2004-4 as REV. PROC. 2004-13

NOVEMBER 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 11/10/2003 in IRB 2003-45 as REV RUL. 2003-114 (released 10/17/2003)

2. Revenue ruling providing the "base period T-Bill rate" as required by section 995(f)(4).
   - PUBLISHED 11/10/2003 in IRB 2003-45 as REV. RUL. 2003-111

3. Revenue ruling setting forth covered compensation tables for the 2004 calendar year for determining contributions to defined benefit plans and permitted disparity.
- PUBLISHED 12/8/2003 in IRB 2003-49 as REV. RUL. 2003-124 (released 11/21/2003)

4. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in November 2003.
- PUBLISHED 11/24/2003 in IRB 2003-47 as NOTICE 2003-74 (released 11/7/2003)

5. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
- PUBLISHED 12/1/2003 in IRB 2003-48 as REV RUL. 2003-121

6. Update of Rev. Proc. 2002-66 regarding adequate disclosure for purposes of the section 6662 substantial understatement penalty and the section 6694 preparer penalty.
- PUBLISHED 11/3/2003 in IRB 2003-44 as REV. PROC. 2003-77

7. News release setting forth cost-of living adjustments effective January 1, 2004, applicable to the dollar limits on benefits under qualified defined benefit pension plans and other provisions affecting certain plans of deferred compensation.
- PUBLISHED 11/10/2003 in IRB 2003-45 as NOTICE 2003-73 (released 10/16/2003 as IR-2003-122)

DECEMBER 2003

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 12/8/2003 in IRB 2003-49 as REV. RUL. 2003-122 (released 11/18/2003)

2. Revenue ruling providing the monthly bond factor amounts to be used by taxpayers who dispose of qualified low-income buildings or interests therein during the period October through December, 2003.
- PUBLISHED 11/17/2003 in IRB 2003-46 as REV. RUL. 2003-117

3. Revenue ruling under section 6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period January through March 2004.
- PUBLISHED 12/29/2003 in IRB 2003-52 as REV. RUL. 2003-126

4. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in December 2003.
- PUBLISHED 12/22/2003 in IRB 2003-51 as NOTICE 2003-80

5. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
- PUBLISHED 12/29/2003 in IRB 2003-52 as REV. RUL. 2003-128

6. Revenue procedure setting forth, pursuant to section 1397E, the maximum face amount of Qualified Zone Academy Bonds that may be issued for each state during 2004.

7. Federal Register notice on Railroad Retirement Tier 2 tax rate.
- PUBLISHED 12/15/2003 in IRB 2003-50 as NOTICE 2003-78 (released 11/25/2003) (also PUBLISHED 11/25/2003 in FR)

JANUARY 2004

1. Revenue procedure updating the procedures for issuing private letter rulings, determination letters, and information letters on specific issues under the jurisdiction of the Chief Counsel.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-1

2. Revenue procedure updating the procedures for furnishing technical advice to certain IRS offices, in the areas under the jurisdiction of the Chief Counsel.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-2

3. Revenue procedure updating the previously published list of "no-rule" issues under the jurisdiction of certain Associates Chief Counsel other than the Associate Chief Counsel (International) on which advance letter rulings or determination letters will not be issued.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-3

4. Revenue procedure updating the previously published list of "no-rule" issues under the jurisdiction of the Associate Chief Counsel (International) on which advance letter rulings or determination letters will not be issued.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-7

5. Revenue procedure updating procedures for furnishing letter rulings, general information letters, etc. in employee plans and exempt organization matters relating to sections of the Code under the jurisdiction of the Office of the Commissioner, Tax Exempt and Government Entities Division.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-4

6. Revenue procedure updating procedures for furnishing technical advice in employee plans and exempt organization matters under the jurisdiction of the Commissioner, Tax Exempt and Government Entities Division.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-5

7. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 1/12/2004 in IRB 2004-2 as REV. RUL. 2004-2
  (released 12/19/2003)

8. Revenue ruling setting forth the prevailing state assumed interest rates provided for the determination of reserves under section 807 for contracts issued in 2003 and 2004.
- WILL BE PUBLISHED 2/23/2004 in IRB 2004-8 as REV. RUL. 2004-14
  (released 1/28/2004)

9. Revenue ruling providing the dollar amounts, increased by the 2003 inflation adjustment for section 1274A.
- PUBLISHED 11/24/2003 in IRB 2003-47 as REV. RUL. 2003-119

10. Revenue ruling setting forth the amount that section 7872 permits a taxpayer to lend to a qualified continuing care facility without incurring imputed interest, adjusted for inflation.
- PUBLISHED 11/24/2003 in IRB 2003-47 as REV. RUL. 2003-118

11. Revenue procedure providing procedures for limitations on depreciation deductions for owners of passenger automobiles first placed in service during the calendar year; amounts to be included in income by lessees of passenger automobiles first leased during the calendar year; and the maximum allowable value of employer-provided automobiles first made available to employees for personal use in the calendar year.

12. Revenue procedure providing the domestic asset/liability percentages and the domestic investment yield percentages for taxable years beginning after December 31, 2002, for foreign companies conducting insurance business in the U.S.

13. Revenue procedure updating procedures for issuing determination letters on the qualified status of employee plans under sections 401(a), 403(a), 409, and 4975.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-6

14. Revenue procedure updating the user fee program as it pertains to requests for letter rulings, determination letters, etc. in employee plans and exempt organizations matters under the jurisdiction of the Office of the Commissioner, Tax Exempt and Government Entities Division.
- PUBLISHED 1/5/2004 in IRB 2004-1 as REV. PROC. 2004-8

15. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in January 2004.

- PUBLISHED 2/2/2004 in IRB 2004-5 as NOTICE 2004-3 (released 1/8/2004)

16. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.
- PUBLISHED 1/26/2004 in IRB 2004-4 as REV. RUL. 2004-7

FEBRUARY 2004

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.
- PUBLISHED 2/9/2004 in IRB 2004-6 as REV. RUL. 2004-9

2. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.

3. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in February 2004.

MARCH 2004

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.

2. Notice providing resident population of the states for determining the calendar year state housing credit ceiling under section 42(h), the private activity bond volume cap under section 146, and the qualified public educational facility bond volume cap under section 142(k).

3. Revenue ruling providing the monthly bond factor amounts to be used by taxpayers who dispose of qualified low-income buildings or interests therein during the period January through March, 2004.
- WILL BE PUBLISHED 2/23/2004 in IRB 2004-8 as REV. RUL. 2004-16

4. Revenue ruling under section 6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period April through June, 2004.

5. Revenue ruling setting forth the terminal charge and the standard industry fare level (SIFL) cents-per-mile rates for the first half of 2004 for use in valuing personal flights on employer-provided aircraft.

6. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in March 2004.

7. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.

APRIL 2004

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.

2. Revenue ruling providing the average annual effective interest rates charged by each Farm Credit Bank District.

3. Notice providing the inflation adjustment factor, nonconventional fuel source

credit, and reference price for the calendar year that determines the availability of the credit for producing fuel from a nonconventional source under section 29.

4. Revenue procedure providing a current list of countries and the dates those countries are subject to the section 911(d)(4) waiver and guidance to individuals who fail to meet the eligibility requirements of section 911(d)(1) because of adverse conditions in a foreign country.

5. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in April 2004.

6. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.

MAY 2004

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.

2. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in May 2004.

3. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.

4. Revenue procedure providing guidance for use of the national and area median gross income figures by issuers of qualified mortgage bonds and mortgage credit certificates in determining the housing cost/income ratio under section 145.

JUNE 2004

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of sections 42, 382, 1274, 1288, and 7520.

2. Revenue ruling providing the monthly bond factor amounts to be used by taxpayers who dispose of qualified low-income buildings or interests therein during the period April through June, 2004.

3. Revenue ruling under section 6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period July through September 2004.

4. Notice providing the calendar year inflation adjustment factor and reference prices for the renewable electricity production credit under section 45.

5. Notice setting forth the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of section 412(c)(7) for plan years beginning in June 2004.

6. Revenue ruling under section 472 providing the Bureau of Labor Statistics price indexes that department stores may use in valuing inventories.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 17, 2004
JS-1174

Treasury International Capital Data For December

Treasury International Capital (TIC) data for December are released today and posted on the U.S. Treasury web site (www.treas.gov/tic). The next release date, which will report on data for January, is scheduled for March 15, 2004.

Domestic Securities

Gross purchases of domestic securities by foreigners were $1,198.8 billion in December, exceeding gross sales of domestic securities by foreigners of $1,118.0 billion during the same month.

Foreign purchases of domestic securities reached $80.8 billion on a net basis in December, relative to $82.4 billion during the previous month. Purchases were largely accounted for by private net flows of $64.4 billion in December. Net private purchases of Corporate Bonds represented the largest inflow from private sources, reaching $19.7 billion in December. Net private purchases of Treasury Bonds and Notes increased to $18.4 billion during the month. Net private purchases of Government Agency Bonds rose for the third consecutive month to $12.9 billion in December. Net private purchases of Equities reached $13.4 billion.

Official net purchases of long-term U.S. securities were $16.4 billion in December, relative to $20.9 billion in November. Official net purchases of Treasury Bonds and Notes of $11.3 billion accounted for the bulk of official inflows in December, down from $18.9 billion the previous month.

Foreign Securities

Gross purchases of foreign securities owned by U.S. residents were $310.1 billion in December, relative to gross sales of foreign securities to U.S. residents of $315.2 billion during the same month.

Gross sales of foreign securities to U.S. residents exceeded purchases by $5.1 billion, highlighting a net U.S. acquisition of $0.1 billion in Foreign Bonds and $5.0 billion in Foreign Equities.

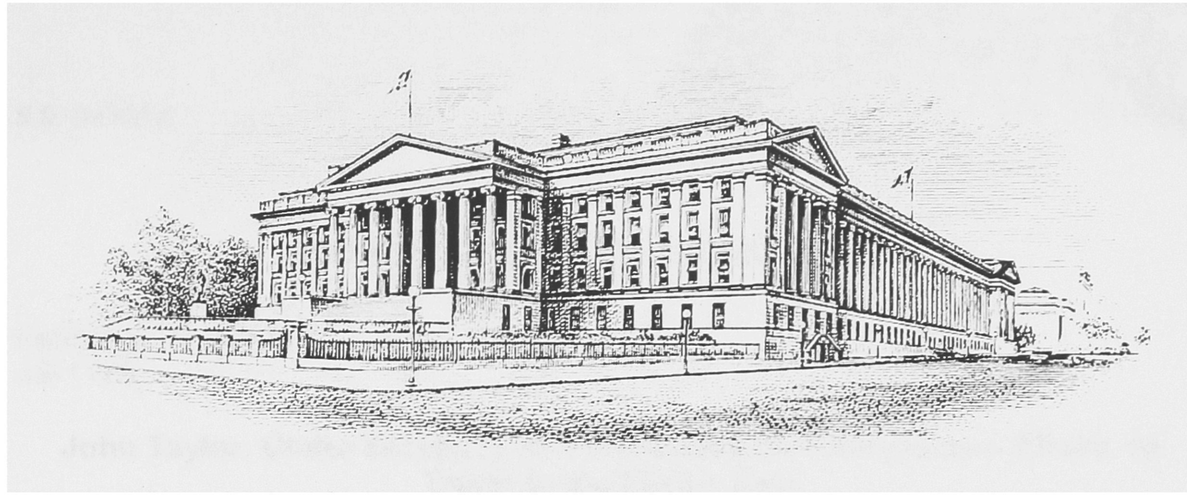
Net Long-Term Securities Flows

Net foreign purchases of long-term securities from U.S. residents were $75.7 billion in December compared with $87.5 billion in November. Net foreign purchases of long-term securities were $707.9 billion in the 12-months through December 2003 as compared to $574.6 million during the twelve months through December 2002.

The full December data set, including adjustments for repayments of principal on asset-backed securities, as well as historical series, can be found on the TIC web site, http://www.treas.gov/tic/.

Related Documents:

- Table 1. Foreigners' Transactions in Long-Term Securities with U.S. Residents



DEPARTMENT OF THE TREASURY
OFFICE OF PUBLIC AFFAIRS

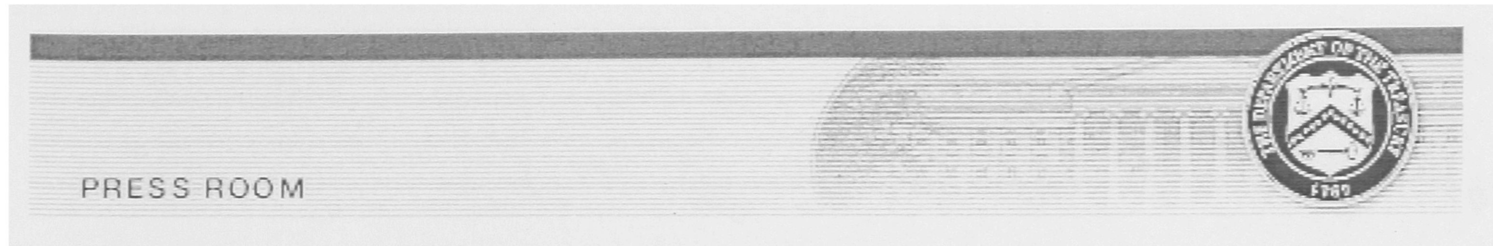
Treasury International Capital
Data Table For December

Table 1. Foreigners' Transactions in Long-Term Securities with U.S. Residents
(Billions of dollars, not seasonally adjusted)

			12 Months Through					
		2001	Dec-02	Dec-03	Sep-03	Oct-03	Nov-03	Dec-03
1	Gross Purchases of Domestic Securities	10,261.8	13,022.9	15,725.9	1,363.0	1,438.4	1,171.1	1,198.8
2	Gross Sales of Domestic Securities	9,740.9	12,475.4	14,981.4	1,347.2	1,397.2	1,088.7	1,118.0
3	**Domestic Securities Purchased, net** (line 1 less line 2) /1	**520.8**	**547.6**	**744.5**	**15.8**	**41.1**	**82.4**	**80.8**
4	**Private, net /2**	**494.2**	**508.3**	**605.0**	**4.3**	**18.3**	**61.5**	**64.4**
5	Treasury Bonds & Notes, net	15.0	112.8	163.7	-2.5	-7.4	14.6	18.4
6	Gov't Agency Bonds, net	146.6	166.6	138.0	-6.3	6.4	9.3	12.9
7	Corporate Bonds, net	218.2	176.7	265.5	19.3	20.3	28.7	19.7
8	Equities, net	114.4	52.2	37.8	-6.2	-1.0	8.9	13.4
9	**Official, net**	**26.7**	**39.3**	**139.5**	**11.5**	**22.9**	**20.9**	**16.4**
10	Treasury Bonds & Notes, net	3.5	7.1	109.3	8.1	19.5	18.9	11.3
11	Gov't Agency Bonds, net	17.4	28.6	24.9	3.0	3.0	1.3	4.4
12	Corporate Bonds, net	3.8	5.6	5.5	0.5	0.7	0.9	0.7
13	Equities, net	2.0	-2.0	-0.2	-0.1	-0.2	-0.2	-0.1
14	Gross Purchases of Foreign Securities	2,557.8	2,640.0	3,535.9	345.7	369.2	321.5	310.1
15	Gross Sales of Foreign Securities	2,577.4	2,613.0	3,572.5	357.2	382.5	316.4	315.2
16	**Foreign Securities Purchased, net** (line 14 less line 15) /3	**-19.6**	**27.0**	**-36.6**	**-11.5**	**-13.3**	**5.1**	**-5.1**
17	Foreign Bonds Purchased, net	30.5	28.5	25.7	-2.7	-5.1	-3.7	-0.1
18	Foreign Equities Purchased, net	-50.1	-1.5	-62.3	-8.9	-8.2	8.8	-5.0
19	**Net Long-Term Securities Flows** (line 3 plus line 16)	**501.2**	**574.6**	**707.9**	**4.3**	**27.8**	**87.5**	**75.7**

/1 Net foreign purchases of U.S. securities (+)
/2 Includes International and Regional Organizations
/3 Net U.S. acquisitions of foreign securities (-)

Source: U.S. Department of the Treasury



FROM THE OFFICE OF PUBLIC AFFAIRS

February 15, 2004
JS-1175

John Taylor, Under Secretary of the Treasury for International Affairs, to Travel to the Middle East

John Taylor, Under Secretary of the Treasury for International Affairs, will travel to several countries in the greater Middle East region from February 14 to February 23, with stops in Afghanistan, Iraq, Israel and the West Bank.

In Afghanistan, he will highlight private sector development, discuss improvements in revenue collection, and talk with other donors on achieving measurable results ahead of the Afghan elections in June. In Iraq, he will review progress on strengthening the financial sector, focusing on monetary policy and the banking sector.

In Israel, he will participate in a meeting of the Joint Economic Development Group with Under Secretary of State Al Larson, and meet with economic policymakers, including Minister Netanyahu and central bank governor Klein. In the West Bank, he will participate in the first meeting of the Palestinian Economic Development Group with Under Secretary of State Al Larson and meet with economic policymakers, including Minister Fayyad.

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FROM THE OFFICE OF PUBLIC AFFAIRS

February 14, 2004
js-1176

Bush Economic Team Announces Trip to Washington, Oregon to Discuss the President's Efforts to Strengthen the Economy and Create Jobs

Department of the Treasury
U.S. Department of Commerce
U.S Department of Labor
U.S. Small Business Administration

FOR IMMEDIATE RELEASE: February 13, 2004
CONTACT: Rob Nichols 202-622-2920

Treasury Secretary John W. Snow, Commerce Secretary Don Evans, Labor Secretary Elaine L. Chao, and Small Business Administration Administrator Hector Barreto will travel to Washington and Oregon on Tuesday, February 17th and Wednesday, February 18th to discuss the state of the economy and the jobs and growth plan - as well as other efforts by President Bush to create jobs, strengthen the economic recovery and increase workers' standards of living.

During the "Jobs and Growth Tour" Secretaries Snow, Evans and Chao and Administrator Barreto will participate in town hall-style meetings, roundtables, and tours in the two states, and will meet with families, workers, manufacturers, local business leaders, economic officials, small business owners, and individual investors.

Secretaries Snow, Evans and Chao conducted a similar tour of Wisconsin and Minnesota in July 2003.

President Bush has said many times, one worker out of work is too many and he wants everyone who wants to work be able to find a job. The President's Jobs and Growth tax relief package helped fuel the strong improvement in the economy during the past two quarters. It raised the level of economic activity, which increases incomes , created hundreds of thousands of new jobs and living standards for American workers , yet there is more to be done.

President Bush during the State of the Union announced new initiatives to strengthen economic growth, further reform education and job training, and address the rising cost of health care. During the two days, the four officials will focus on these new initiatives and specifically what we can do to make sure people are prepared for the jobs for the 21st century.

More than two million taxpayers in Washington, and more than one million taxpayers in Oregon, will have lower income tax bills in 2004 as a result of President Bush's Jobs and Growth Act.

During the two days, the officials will participate in events in Spokane, Richland and Yakima, Washington and Portland and Eugene, Oregon.

A detailed schedule will be released on Monday, February 16, 2004 on www.treas.gov.

Interview requests should be directed to Ginny Ward at 202-482-1008.

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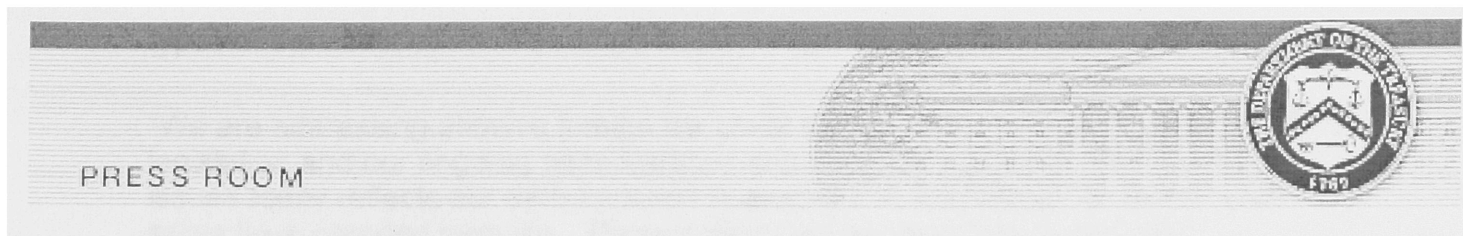

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 17, 2004
JS--1177

Treasury and IRS issue Guidance on Abusive Foreign Tax Credit Transactions

Today, the Treasury Department and the IRS issued two notices concerning transactions intended to generate foreign tax credits for U.S. taxpayers. Notice 2004-19 describes the administrative and regulatory approaches the Treasury and IRS are using to address foreign tax credit transactions that create results inconsistent with the purpose of the foreign tax credit rules. Notice 2004-19 also discusses the legislation proposed in the President's FY 2005 Budget. The legislation would provide additional statutory rules disallowing foreign tax credits in appropriate circumstances and would grant Treasury regulatory authority to ensure that the mechanical foreign tax credit rules cannot be used to achieve results that do not reflect the economic effect of the transactions.

Notice 2004-19 reflects careful consideration of Notice 98-5. Notice 98-5 described an approach for disallowing foreign tax credits based on a comparison of economic profit to the claimed tax benefits and stated that this approach would be implemented through regulations. Treasury and the IRS have decided not to issue regulations as described in Notice 98-5. This decision was influenced by recent court cases involving foreign tax credit transactions that clearly produced results inconsistent with the purpose of the foreign tax credit rules. The courts held that the approach taken in Notice 98-5 did not support the IRS's proposed disallowance of foreign tax credits in those cases. Treasury and the IRS disagree strongly with the result in those cases, but have concluded that the approach described in Notice 98-5 is unlikely to be an effective tool for addressing transactions that abuse the foreign tax credit rules. Accordingly, Notice 2004-19 withdraws Notice 98-5, and describes the approaches Treasury and the IRS are using to address transactions and arrangements structured to give rise to inappropriate foreign tax credit results.

Notice 2004-20 halts a specific transaction designed to generate credits for foreign taxes paid on gain that is not subject to tax in the United States. The claimed result of the transaction is a foreign tax credit but no corresponding income and U.S. tax for the U.S. taxpayer.

The transaction involves a purported acquisition of stock of a foreign target corporation by a domestic corporation, an accompanying election under section 338, and a prearranged plan to sell the target corporation's assets in a transaction that gives rise to foreign tax without corresponding income for U.S. tax purposes. This transaction does not produce the foreign tax credit benefits claimed to be generated. Under Notice 2004-20, this transaction, and any transaction that is substantially similar, are identified as "listed transactions" that are subject to disclosure, list-keeping, and registration requirements.

"The foreign tax credit serves the important purpose of eliminating potential double taxation. It was never intended to eliminate tax altogether," stated Treasury Assistant Secretary for Tax Policy Pam Olson. "Transactions structured so the taxpayer incurs foreign taxes without any corresponding U.S. tax liability because the underlying income is not recognized for U.S. tax purposes do not give rise to the double taxation that is the economic basis for the foreign tax credit. These

types of transactions should not generate foreign tax credits."

"We are addressing abusive foreign tax credit transactions through proposed legislation and our ongoing administrative and regulatory actions. The guidance issued today reflects our determination to ensure that the foreign tax credit rules serve their intended purpose. These notices are an important part of our comprehensive efforts to address tax shelter transactions," continued Assistant Secretary Olson.

"The Treasury Department and the IRS will continue to use all of the tools available to stem abusive foreign tax credit transactions. In addition, we urge Congress to pass the legislation proposed in the President's Budget to ensure the government has additional tools to prevent abuse in this area," concluded Assistant Secretary Olson.

Related Documents:

- Notice 2004-19
- Notice 2004-20

FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
2004-3-1-11-11-2-20848

U.S. International Reserve Position

The Treasury Department today released U.S. reserve assets data for the latest week. As indicated in this table, U.S. reserve assets totaled $86,014 million as of the end of that week, compared to $85,368 million as of the end of the prior week.

I. Official U.S. Reserve Assets *(in US millions)*

	January 30, 2003			February 6, 2004		
TOTAL		85,368			86,014	
1. Foreign Currency Reserves [1]	Euro	Yen	TOTAL	Euro	Yen	TOTAL
a. Securities	8,386	14,862	23,248	8,570	14,900	23,469
Of which, issuer headquartered in the U.S.			0			0
). Total deposits with:						
.i. Other central banks and BIS	13,606	2,986	16,592	13,876	2,993	16,869
.ii. Banks headquartered in the U.S.			0			0
.ii. Of which, banks located abroad			0			0
iii. Banks headquartered outside the U.S.			0			0
iii. Of which, banks located in the U.S.			0			0
IMF Reserve Position [2]			21,887			21,981
Special Drawing Rights (SDRs) [2]			12,598			12,652
Gold Stock [3]			11,043			11,043
Other Reserve Assets			0			0

II. Predetermined Short-Term Drains on Foreign Currency Assets

	January 30, 2003			February 6, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
'eign currency loans and securities			0			0

ǀregate short and long positions in forwards and futures in foreign currencies vis-à-vis the U.S. dollar:

2.a. Short positions	0	0
2.b. Long positions	0	0
3. Other	0	0

III. Contingent Short-Term Net Drains on Foreign Currency Assets

	January 30, 2003			February 6, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
1. Contingent liabilities in foreign currency			0			0
1.a. Collateral guarantees on debt due within 1 year						
1.b. Other contingent liabilities						
2. Foreign currency securities with embedded options			0			0
3. Undrawn, unconditional credit lines			0			0
3.a. With other central banks						
.b. With banks and other financial institutions						
leadquartered in the U.S.						
.c. With banks and other financial institutions						
'eadquartered outside the U.S.						
Aggregate short and long positions of ptions in foreign						
ırrencies vis-à-vis the U.S. dollar			0			0
. Short positions						
.1. Bought puts						
.2. Written calls						
Long positions						
1. Bought calls						
2. Written puts						

Notes:

des holdings of the Treasury's Exchange Stabilization Fund (ESF) and the Federal Reserve's System Open Market Account), valued at current market exchange rates. Foreign currency holdings listed as securities reflect marked-to-market values, posits reflect carrying values. Foreign Currency Reserves for the latest week may be subject to revision. Foreign Currency

Reserves for the prior week are final.

2/ The items, "2. IMF Reserve Position" and "3. Special Drawing Rights (SDRs)," are based on data provided by the IMF and are valued in dollar terms at the official SDR/dollar exchange rate for the reporting date. The entries for the latest week reflect any necessary adjustments, including revaluation, by the U.S. Treasury to IMF data for the prior month end.

3/ Gold stock is valued monthly at $42.2222 per fine troy ounce.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
2004-2-19-17-10-2-26860

U.S. International Reserve Position

The Treasury Department today released U.S. reserve assets data for the latest week. As indicated in this table, U.S. reserve assets totaled $85,909 million as of the end of that week, compared to $86,096 million as of the end of the prior week.

I. Official U.S. Reserve Assets *(in US millions)*

	February 6, 2003			February 13, 2004		
TOTAL		86,096			85,909	
1. Foreign Currency Reserves [1]	**Euro**	**Yen**	**TOTAL**	**Euro**	**Yen**	**TOTAL**
a. Securities	8,386	14,862	23,248	8,617	14,896	23,513
Of which, issuer headquartered in the U.S.			0			0
. Total deposits with:						
i. Other central banks and BIS	13,606	2,986	16,592	13,944	2,293	16,237
ii. Banks headquartered in the U.S.			0			0
ii. Of which, banks located abroad			0			0
iii. Banks headquartered outside the U.S.			0			0
ii. Of which, banks located in the U.S.			0			0
IMF Reserve Position [2]			22,561			22,288
Special Drawing Rights (SDRs) [2]			12,652			12,829
Gold Stock [3]			11,043			11,043
Other Reserve Assets			0			0

II. Predetermined Short-Term Drains on Foreign Currency Assets

	January 6, 2003			February 13, 2004		
	Euro	**Yen**	**TOTAL**	**Euro**	**Yen**	**TOTAL**
ign currency loans and securities			0			0
egate short and long positions in forwards and futures in foreign currencies vis-à-vis the U.S. dollar:						

2.a. Short positions			0			0
2.b. Long positions			0			0
3. Other			0			0

III. Contingent Short-Term Net Drains on Foreign Currency Assets

	February 6, 2003			February 13, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
1. Contingent liabilities in foreign currency			0			0
1.a. Collateral guarantees on debt due within 1 year						
1.b. Other contingent liabilities						
2. Foreign currency securities with embedded options			0			0
3. Undrawn, unconditional credit lines			0			0
3.a. With other central banks						
.b. With banks and other financial institutions						
leadquartered in the U.S.						
c. With banks and other financial institutions						
eadquartered outside the U.S.						
Aggregate short and long positions of tions in foreign						
rrencies vis-à-vis the U.S. dollar			0			0
. Short positions						
.1. Bought puts						
2. Written calls						
Long positions						
1. Bought calls						
2. Written puts						

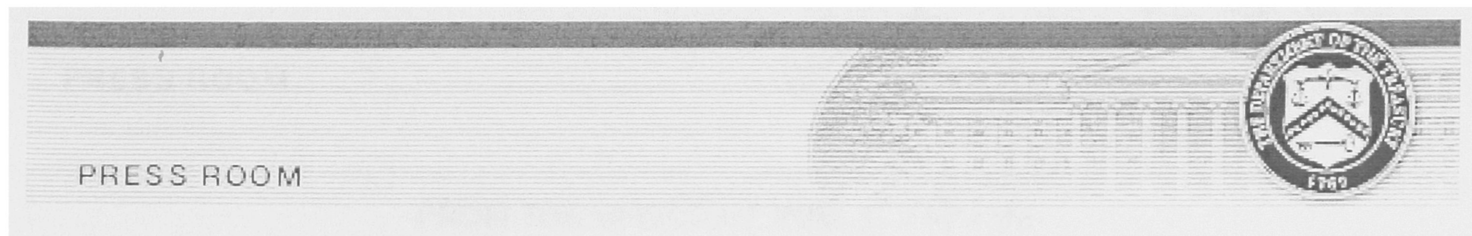
Notes:

des holdings of the Treasury's Exchange Stabilization Fund (ESF) and the Federal Reserve's System Open Market Account), valued at current market exchange rates. Foreign currency holdings listed as securities reflect marked-to-market values, and s reflect carrying values. Foreign Currency Reserves for the latest week may be subject to revision. Foreign Currency

Reserves for the prior week are final.

2/ The items, "2. IMF Reserve Position" and "3. Special Drawing Rights (SDRs)," are based on data provided by the IMF and are valued in dollar terms at the official SDR/dollar exchange rate for the reporting date. The entries for the latest week reflect any necessary adjustments, including revaluation, by the U.S. Treasury to IMF data for the prior month end.

3/ Gold stock is valued monthly at $42.2222 per fine troy ounce.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 17, 2004
JS-1178

Bush Economic Team Visits Workers, Business Owners, Families in Washington

President's Efforts to Strengthen the Economy and Create Jobs Discussed

FOR IMMEDIATE RELEASE: February 17, 2004
CONTACT: Rob Nichols at 202-622-2920

Treasury Secretary John W. Snow, Commerce Secretary Don Evans, Labor Secretary Elaine L. Chao, and Small Business Administrator Hector Barreto traveled through Washington on a bus today, making stops to discuss the state of the economy and the President's jobs and growth plan as well as other efforts by President Bush to create jobs, strengthen the economic recovery and increase workers' standards of living.

"There is no better way to get a feel for how the economy is doing, and what people really need from their government, than to get out here and visit with folks," Snow said. "We're hearing that tax cuts have worked well so far for businesses and families in Washington – and that taxes shouldn't be increased now, just when progress is being made. We intend to bring that message back to Capitol Hill," he added.

More than two million taxpayers in Washington will have lower income tax bills in 2004 as a result of President Bush's Jobs and Growth Act.

"This administration will not be satisfied until everyone who wants to work can find a job. There are tremendous resources available to help workers transitioning between jobs and we want workers in Washington and Oregon to know about them -- there is something for everyone." said Secretary of Labor Elaine L. Chao."

Secretaries Snow, Evans and Chao and Administrator Barreto visited the Spokane Intercollegiate Research and Technology Institute foundation this morning, talked with women business owners in Richland this afternoon, and met with families at a Mexican restaurant in Yakima at the end of the day. At each stop, participants were encouraged to give a report on how the economy is doing in their community, and make suggestions for ways to increase growth and job creation.

The bus tour will continue in Oregon tomorrow. Secretaries Snow, Evans and Chao conducted a similar tour of Wisconsin and Minnesota in July 2003.

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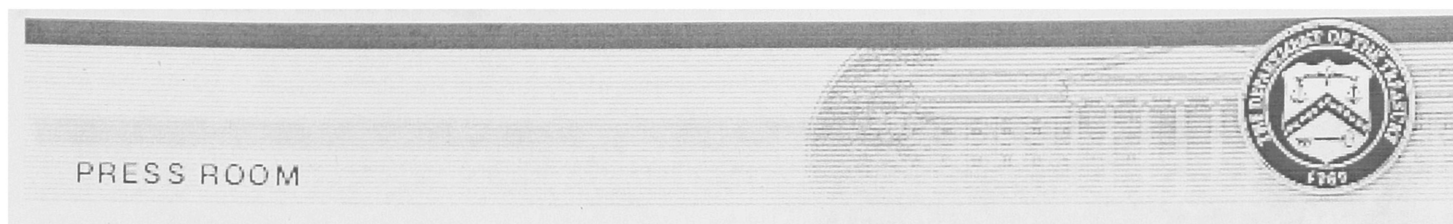
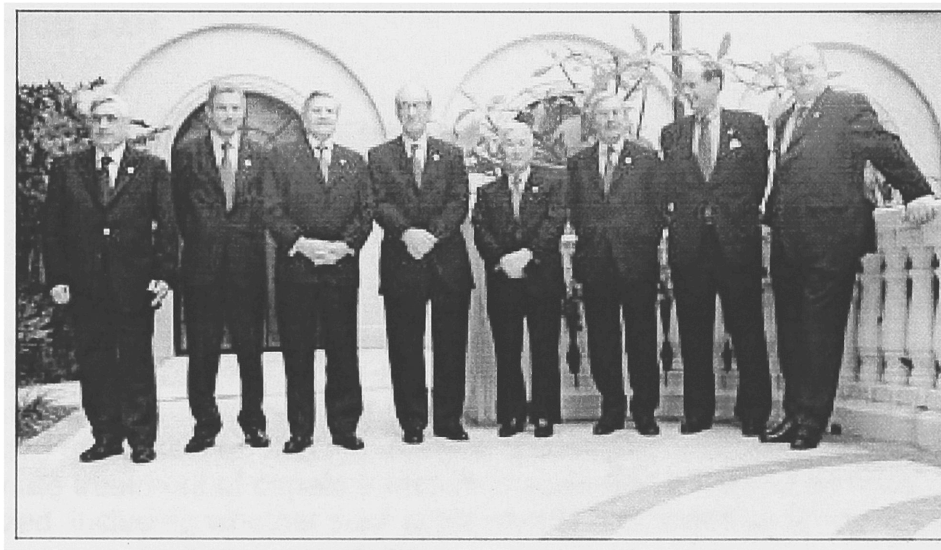


FROM THE OFFICE OF PUBLIC AFFAIRS

February 8, 2004
JS-1179

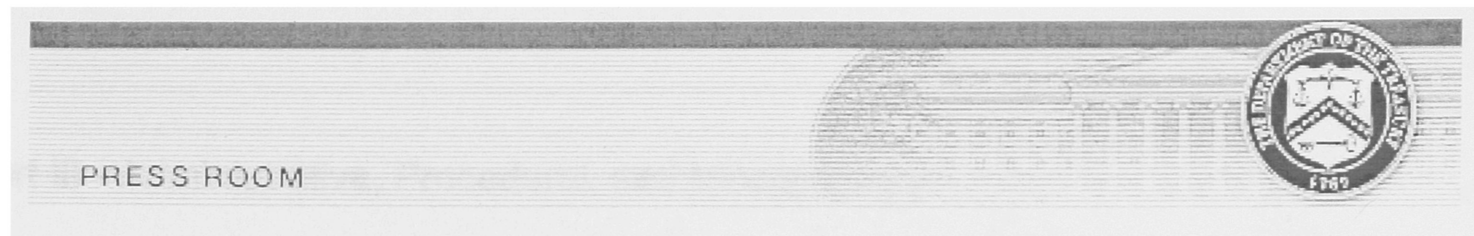
Photo: G7 Governors



Media Contact

All media queries should be directed to
The Press Office at (202) 622-2960.
Only call this number if you are a member of the media.

High Resolution Image



FROM THE OFFICE OF PUBLIC AFFAIRS

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February 19, 2004
JS-1180

Treasury Issues Notice Concerning Treatment of Certain Capitalized Transaction Costs

The Treasury Department and IRS issued a notice today announcing their intention to propose regulations regarding the treatment of amounts that facilitate certain tax-free and taxable transactions and other restructurings, and that are required to be capitalized under section 263. The notice requests comments regarding the appropriate treatment of certain transaction costs that are required to be capitalized, including whether such costs should be treated as giving rise to a new asset the basis of which is amortizable.

"The proper treatment of amounts incurred to facilitate certain transactions has been the subject of disputes between taxpayers and the IRS in recent years," stated Acting Treasury Assistant Secretary for Tax Policy Greg Jenner. "This notice is the first step toward providing clear and administrable rules."

Related Documents:

- Notice 2004-18

Part III - Administrative, Procedural, and Miscellaneous

Request for Comments Concerning the Treatment of Amounts Required to Be Capitalized in Certain Transactions to which § 1.263(a)-5 Applies

Notice 2004-18

On December 22, 2003, the Treasury Department and Internal Revenue Service issued final regulations (T.D. 9107; 69 FR 436) under § 263(a) of the Internal Revenue Code requiring capitalization of certain amounts that facilitate the creation or acquisition of an intangible asset and under § 167 providing a 15-year safe harbor amortization period for certain intangible assets described in § 263(a). The final regulations under § 263(a) also provide guidance on the treatment of amounts required to be capitalized under § 263(a) in certain acquisitions of a trade or business. For example, § 1.263(a)-5(g)(2) provides that amounts required to be capitalized by an acquirer in an acquisition, merger, or consolidation that is not described in § 368 are added to the basis of the acquired assets (in the case of a transaction that is treated as an acquisition of the assets of the target for federal income tax purposes) or the acquired stock (in the case of a transaction that is treated as an acquisition of the stock of the target for federal income tax purposes).

The final regulations under § 263(a) do not address the treatment of amounts required to be capitalized in certain other transactions to which the regulations apply (for example, amounts required to be capitalized in tax-free transactions, costs of a target in a taxable stock acquisition, and stock issuance costs). The preamble to the final regulations states that the Service and Treasury Department intend to issue separate guidance to address the treatment of these amounts and will consider at that time whether such amounts should be eligible for the 15-year safe harbor amortization period described in § 1.167(a)-3(b).

The Service and Treasury Department are aware that there is continuing controversy as to the proper treatment of certain costs that facilitate certain tax-free and taxable transactions and other restructurings and that are required to be capitalized under § 263(a) and § 1.263(a)-5. The Service and Treasury Department also are aware that, under current law, capitalized costs that facilitate tax-free and taxable transactions that are similar may be treated differently. For example, § 1.263(a)-5(g)(2) provides that the acquirer's capitalized transaction costs that facilitate a taxable asset acquisition increase the basis of the acquired assets. Some commentators, however, have expressed differing views as to how an acquirer's capitalized transaction costs that facilitate a tax-free asset acquisition are treated. In addition, the Service and Treasury Department are aware that, under current law, similar costs may be treated differently depending on which party incurs the costs. Commentators have suggested that capitalized transaction costs incurred by an acquirer and target to facilitate a tax-free stock acquisition may be treated differently.

To reduce the prospect of future controversy, the Service and Treasury Department intend to propose regulations to address the treatment of amounts that facilitate certain tax-free and taxable transactions and other restructurings and that are required to be capitalized under § 263(a) and § 1.263(a)-5. The Service and Treasury Department intend to develop a set of rules that are clear and administrable.

The Service and Treasury Department are considering the treatment of capitalized costs that facilitate the following transactions:

(1) Tax-free asset acquisitions and dispositions (for example, reorganizations under § 368(a)(1)(A), (C), (D), (G));

(2) Taxable asset acquisitions and dispositions (*see* § 1.263(a)-5(g) for the treatment of certain transaction costs in taxable asset acquisitions);

(3) Tax-free stock acquisitions and dispositions (for example, reorganizations under § 368(a)(1)(B));

(4) Taxable stock acquisitions and dispositions (*see* § 1.263(a)-5(g) for the treatment of certain transaction costs in taxable stock acquisitions);

(5) Tax-free distributions of stock (for example, distributions of stock to which § 305(a) or § 355(a) applies);

(6) Tax-free distributions of property (for example, distributions to which §§ 332 and 337 apply);

(7) Taxable distributions of property (for example, distributions to which §§ 331 and 336 apply and distributions of stock to which § 311 applies);

(8) Organizations of corporations, partnerships, and entities that are disregarded as separate from their owner (for example, transfers described in § 351 or § 721);

(9) Corporate recapitalizations (for example, reorganizations under § 368(a)(1)(E));

(10) Reincorporations of corporations in a different state (for example, in a reorganization under § 368(a)(1)(F)); and

(11) Issuances of stock.

There are specific issues raised by each of these types of transactions. The Service and Treasury Department previously have requested comments more generally on the treatment of capitalized costs that facilitate certain of these transactions. In this Notice,

the Service and Treasury Department request additional comments, including comments focusing on the following issues.

ISSUES ON WHICH COMMENTS ARE REQUESTED

(1) Treatment of capitalized costs. Section 263(a) and the regulations thereunder require that certain amounts that facilitate the transactions listed above be capitalized. The Service and Treasury Department request comments regarding whether the particular capitalized costs that facilitate transactions for which the Service and Treasury Department are considering guidance should (a) increase the basis of a particular asset or assets (and, if the basis of multiple assets should be increased, the methodology for allocating the costs among the assets), (b) be treated as giving rise to a new asset the basis of which may not be amortized, (c) be treated as giving rise to a new asset the basis of which may be amortizable, (d) reduce an amount realized, or (e) be treated as an adjustment to equity. To the extent that capitalized costs should be treated as giving rise to a new asset the basis of which may be amortizable, the Service and Treasury Department request comments regarding the appropriate amortizable useful life. For example, an appropriate amortizable useful life might be 15 years, a useful life consistent with that afforded to certain intangibles under § 1.167(a)-3(b) and § 197. Additionally, if such costs are treated as giving rise to a new, amortizable asset, the Service and Treasury Department also request comments as to the treatment of such costs if a specific event (e.g., a liquidation) occurs prior to the expiration of the amortization period.

(2) Consistent treatment of capitalized costs that facilitate similar taxable and tax-free transactions. The regulations promulgated under § 263(a) provide rules regarding the treatment of amounts that facilitate a taxable acquisition of stock and assets and a taxable disposition of assets. The Service and Treasury Department request comments regarding whether, as a policy matter, capitalized costs that facilitate a tax-free transaction should be treated in the same manner as the capitalized costs that facilitate a similar taxable transaction.

(3) Consistent treatment of all capitalized costs that facilitate a transaction. The Service and Treasury Department request comments regarding whether, as a policy matter, capitalized costs that facilitate a transaction, regardless of the type of cost and the party to the transaction that incurs such cost, should be treated similarly.

DATES: Written and electronic comments must be submitted by April 19, 2004.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (Notice 2004-18), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:LPD:PR (Notice 2004-18), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue N.W., Washington, DC. Alternatively, taxpayers may send submissions electronically directly to the Service at:

Notice.comments@irscounsel.treas.gov All materials submitted will be available for public inspection and copying.

FOR FURTHER INFORMATION CONTACT: Concerning submissions, Guy Traynor (202) 622-7180; concerning this notice, Andrew J. Keyso, (202) 622-4800 (not toll-free numbers).

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 19, 2004
js-1181

Treasury takes action against FARC/AUC Narco-Terrorist Leaders in continued effort to Halt Narcotics Trafficking

In another important effort in the battle against narcotics trafficking, the Treasury Department took action today against leaders and key figures of the Colombian narco-terrorist organizations, the Revolutionary Armed Forces of Colombia (Fuerzas Armadas Revolucionarias de Colombia, "FARC") and the United Self-Defense Forces of Colombia (Autodefensas Unidas de Colombia, "AUC").

The Treasury's Office of Foreign Assets Control (OFAC) has added the names of FARC leaders, including Pedro Antonio Marin and Jorge Briceno Suarez, key AUC figures, including Carlos Castano Gil and Salvatore Mancuso Gomez and AUC front companies to the list of "Tier II" persons designated under the Foreign Narcotics Kingpin Designation Act (Kingpin Act). The 40 Colombian names added to the Kingpin Act list include 19 FARC individuals, 18 individuals associated with the AUC and three front companies connected to the AUC. These 40 persons are subject to the economic sanctions imposed against foreign drug cartels under the Kingpin Act.

The OFAC action prohibits U.S. individuals and companies from doing business with the 40 designated persons and blocks their assets found in U.S. jurisdiction. Today's designations comprise the first actions by Treasury against the operatives and fronts of the FARC and the AUC; and they are part of Treasury's plan to further identify, expose, isolate and incapacitate these Colombian narco-terrorists and their support networks.

These Kingpin Act designations reinforce the reality that the FARC and the AUC are not simply terrorist/guerrilla organizations fighting within Colombia to achieve political agendas. They are part and parcel of the narcotics production and export threat to the United States, as well as Europe and other countries of Latin America.

The FARC and the AUC organizations were designated by President Bush as Significant Foreign Narcotics Traffickers on May 29, 2003. As the White House announced at that time, "This action underscores the President's determination to pursue narco-terrorists. This action also underscores the President's determination to do everything possible to fight drug traffickers, undermine their operations and end the suffering that trade in illicit drugs inflicts on Americans and other people around the world."

Under President Bush's Executive Order 13224, both the FARC and the AUC were named as Specially Designated Global Terrorists in October 2001. Previously, the FARC, in October 1997, and the AUC, in September 2001, had been identified as Foreign Terrorist Organizations under the Antiterrorism and Effective Death Penalty Act.

The list of Tier II individuals includes the supreme leader of the FARC, Pedro Antonio Marin, the leaders of the FARC Secretariat, its governing body, certain key FARC commanders, an international representative of the FARC, and key FARC members engaged in narcotics trafficking or the murder of U.S. citizens. The list of Tier II individuals also includes a number of AUC key figures, AUC financial managers and key AUC members connected with narcotics trafficking. Three

businesses that are run on behalf of the AUC are also being designated.

This action is part of the ongoing interagency effort to carry out the mandate of the Kingpin Act, which applies economic sanctions against foreign narcotics trafficking kingpins worldwide. It reflects the increasing cooperation, coordination and integration among these agencies in the battle against international narcotics trafficking and narco-terrorism.

A total of 104 organizations, individuals and businesses in 12 foreign countries are now designated under the Kingpin Act. In addition to the prohibitions on transactions and blocking of assets subject to U.S. jurisdiction, penalties under the Kingpin Act range from civil penalties of up to $1,075,000 per violation to more severe criminal penalties. Criminal penalties for corporate officers are up to 30 years in prison and fines up to $5,000,000. Criminal fines for corporations are up to $10,000,000. Other individuals face up to ten years in prison for criminal violations of the Kingpin Act.

This and other Tier II actions under the Kingpin Act are coordinated by the Department of Treasury with the Department of State, the Department of Justice, the Department of Defense, the Department of Homeland Security, the Central Intelligence Agency, the Drug Enforcement Administration and the Federal Bureau of Investigation.

The list of individuals named by OFAC as Tier II designations today is attached and available at www.treas.gov/ofac, as is the entire list of Kingpin Act designations. Today's list will be published in the Federal Register at a later date.

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REPORTS

- FARC – Foreign Narcotics Kingpin Designation Act – Tier II
- AUC – Foreign Narcotics Kingpin Designation Act – Tier II

Foreign Narcotics Kingpin Designation Act - Tier II

Revolutionary Armed Forces of Colombia (FARC)

(19 Individuals)

Department of the Treasury
Office of Foreign Assets Control

February 2004

FARC Designated by the President as a Significant Foreign Narcotics Trafficker on May 29, 2003

Pedro Antonio Marin
"Manuel Marulanda"
"Tirofijo"
FARC Supreme Leader
Indicted in Colombia

FARC SECRETARIAT

Milton de Jesus Toncel Redondo
"Joaquin Gomez"
Secretariat Member
FARC Commander
Indicted in Colombia

Rodrigo Londono Echeverry
"Timoleon Jimenez"
Secretariat Member
FARC Commander
Indicted in Colombia

Noel Mata Mata
"Efrain Guzman"
Secretariat Member
FARC Commander
Indicted in Colombia

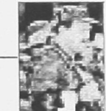
Luciano Marin Arango
"Ivan Marquez"
Secretariat Member
FARC Commander
Indicted in Colombia

Guillermo Leon Saenz Vargas
"Alfonso Cano"
Secretariat Member
FARC Commander
Indicted in Colombia

Luis Edgar Devia Silva
"Raul Reyes"
Secretariat Member
Indicted in Colombia

Jorge Briceno Suarez
"Mono Jojoy"
Secretariat Member
Senior FARC Military Commander
U.S. Indictment (Narcotics & Kidnapping)
Indicted in Colombia

Brothers



German Briceno Suarez
"Granobles"
FARC Commander
U.S. Indictment (Murder)
Indicted in Colombia

Juvenal Ovidio Ricardo Palmera Pineda
"Simon Trinidad"
FARC Commander
Captured in Ecuador - January 2004
In Colombian Custody
Indicted in Colombia

Luis Alberto Alban Burbano
FARC International Representative
Indicted in Colombia

Henry Castellanos Garzon
"Romaña"
FARC Front Commander
U.S. Indictment (Kidnapping)
Indicted in Colombia

Jose Benito Cabrera Cuevas
"Fabian Ramirez"
FARC Commander
Indicted in Colombia

Tomas Molina Caracas
"Negro Acacio"
16th Front Commander
U.S. Indictment (Narcotics & Kidnapping)
Indicted in Colombia

Jorge Torres Victoria
"Pablo Catatumbo"
FARC Central General Staff member
FARC Commander
Indicted in Colombia

Nelson Vargas Rueda
FARC member
Captured in Colombia
In U.S. Custody
U.S. Indictment (Murder)

Gustavo Bocota Aguablanca
FARC Member
U.S. Indictment (Murder)

Eugenio Vargas Perdomo
"Carlos Bolas"
FARC Member
Captured in Suriname - June 2002
In U.S. Custody
U.S. Indictment (Narcotics)

Ties to Brazilian narcotics traffickers Luis Fernando Da Costa and Leonardo Dias Mendonca, previously designated by the President as Tier I Kingpins

Oscar Caracas Viveros
FARC Member
U.S. Indictment (Narcotics)

Foreign Narcotics Kingpin Designation Act - Tier II

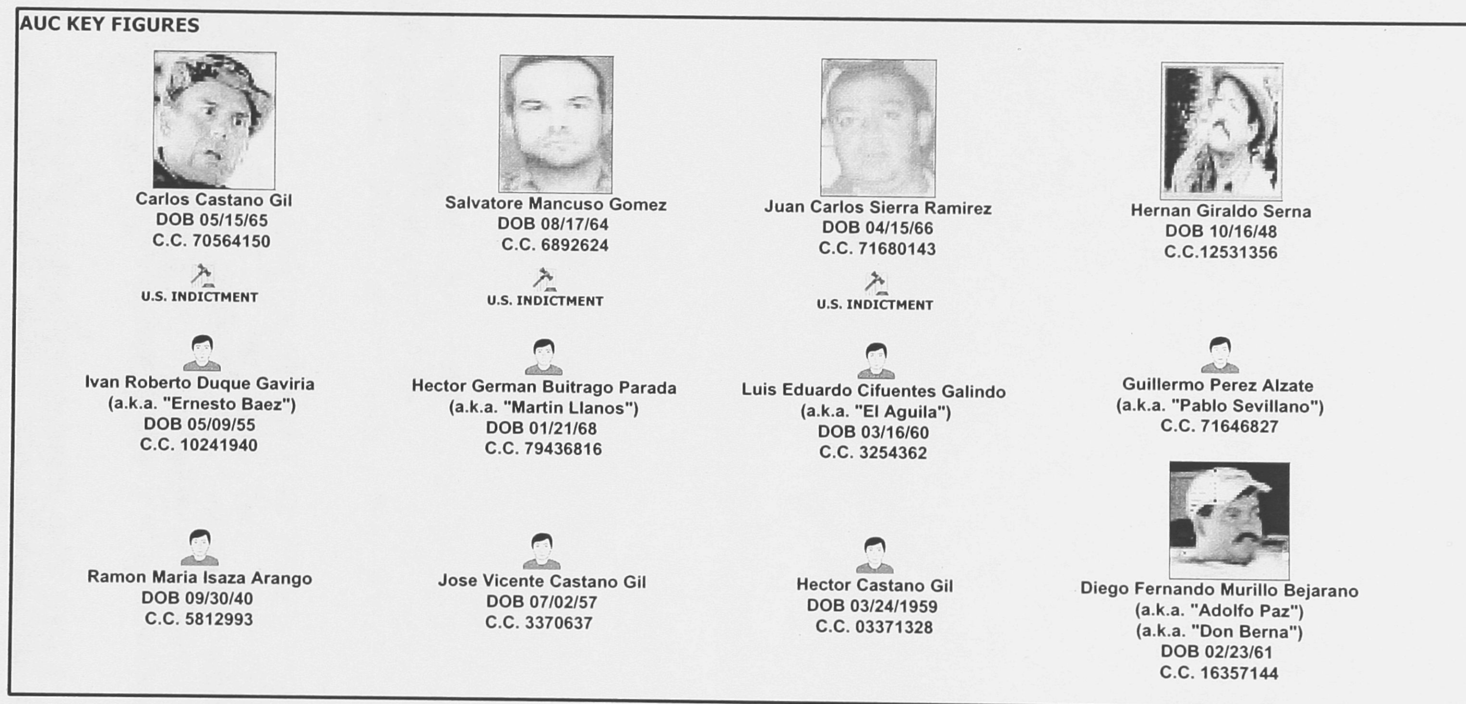
United Self-Defense Forces of Colombia (AUC)

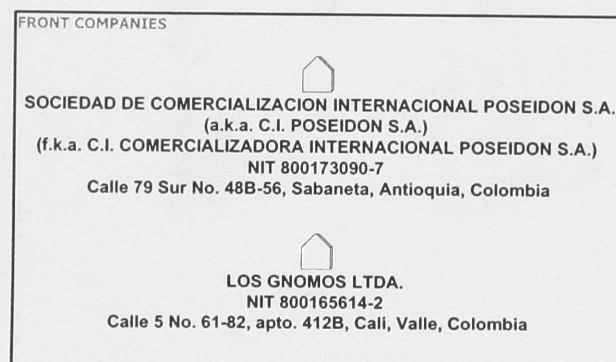
(18 Individuals & 3 entities)

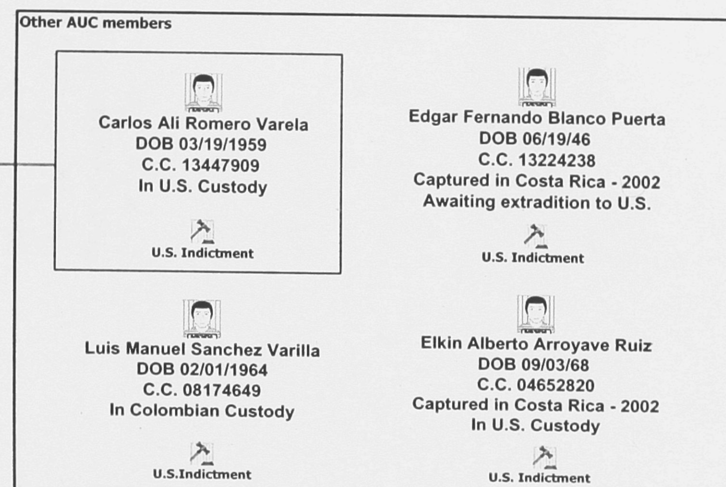
Department of the Treasury
Office of Foreign Assets Control

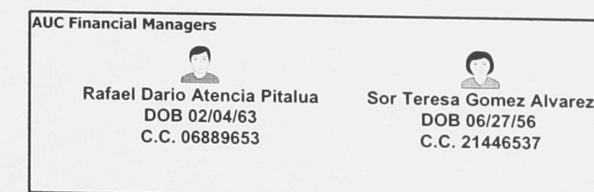
February 2004

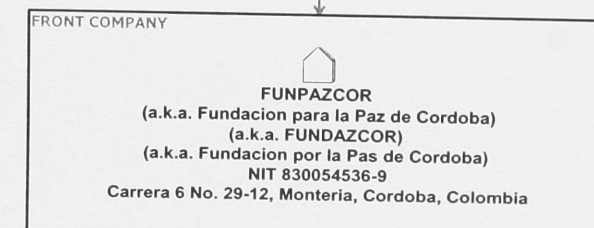
AUC Designated by the President as a Significant Foreign Narcotics Trafficker on May 29, 2003











FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
JS-1182

MEDIA ADVISORY:
Zarate, Treasury Officials to Brief on Designation of FARC/AUC NARCO-Terrorist Leaders

The Treasury Department today will hold a briefing with reporters to discuss the action taken against leaders and key figures of the Colombian narco-terrorist organizations, the Revolutionary Armed Forces of Colombia (Fuerzas Armadas Revolucionarias de Colombia, "FARC") and the United Self-Defense Forces of Colombia (Autodefensas Unidas de Colombia, "AUC").

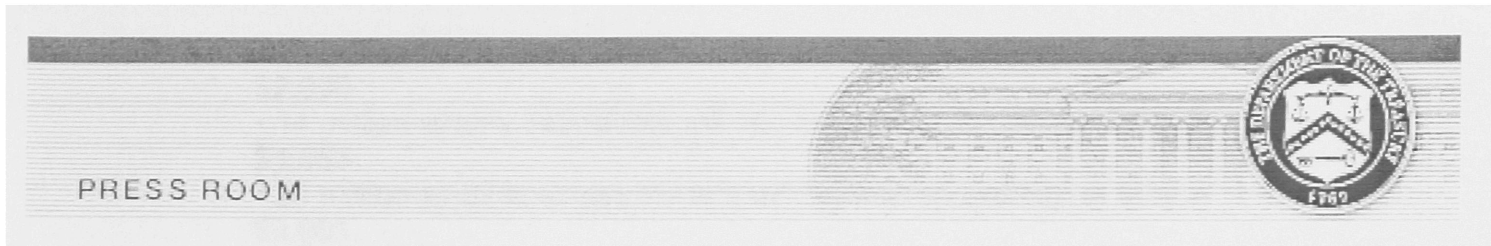
WHO: Juan C. Zarate, Deputy Assistant Secretary, Executive Office for Terrorist Financing and Financial Crimes Richard Newcomb, Director, Office of Foreign Assets Control (OFAC) Richard Speier, Internal Revenue Service, Deputy Chief of Criminal Investigation

WHAT: Pen and Pad Briefing – no cameras will be admitted

WHEN: 2:00 pm EST

WHERE: Department of Treasury – Media Room (4121)

Media without Treasury press credentials, including media with White House credentials, planning to attend should contact Frances Anderson in Treasury's Office of Public Affairs at (202) 528-9086. Please be prepared to provide her with the following information: name, social security number and date of birth by noon EST.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
JS-1201

Treasury Releases New Data On The Benefits Of The Jobs And Growth Tax Relief Reconciliation Act

(Revised)

The Department of the Treasury today released new figures demonstrating that because of the President's tax relief package enacted last May, an additional $50 billion dollars will remain in the hands of American taxpayers through higher refunds and lower tax payments this spring. The total refunds Americans will receive this spring will increase to about $195 billion.

- As a result of the tax cuts in 2003, Treasury expects that a record number of individuals will receive refunds this year.
- Treasury expects that the average refund will be $300 higher than had the Jobs & Growth Tax Relief Act had not been enacted.
- The President's 2003 tax relief is expected to increase refunds received by Americans by about $37 billion more than if the Jobs & Growth Tax Relief Act had not been enacted, from approximately $158 billion to $195 billion.
- The tax relief is expected to decrease the amount that Americans who must make tax payments when filing their tax returns this spring by approximately $13 billion, from $85 billion to $72.5 billion.
- Taken together the higher tax refunds and lower tax payments are expected to put an additional $50 billion in the hands of American taxpayers this spring.

In addition, Treasury's data shows that American families will see a significant reduction in their tax burden because of the tax relief packages that the President has signed since taking office. The President's 2001 and 2003 tax cuts mean that in 2004:

- Americans will receive a total of $232 billion in tax relief in 2004.
- $176 billion in tax relief will stay in the hands of American families and small businesses to help then save and invest.
- Every American who would have paid income taxes before the tax relief was enacted in 2001 will receive a tax cut in 2004.

The President's Tax Cuts Mean Significant Tax Relief for Working American Families Expanding the 10% bracket and doubling the child tax credit will benefit low income Americans

- Nearly 5 million taxpayers, including 4 million taxpayers with children, will have their income tax liability completely eliminated in 2004.
- Low-income families will also benefit from provisions that make the child credit refundable for more families and reduce marriage penalties caused by the EITC. 111 million individuals and families will receive an average tax cut of $1,586 in 2004 because of the tax cutes of 2001 and 2003.

- 49 million married couples will have an average tax cut of $2,602.

• 43 million families with children will receive an average tax cut of $2,090.
• 14 million elderly individuals will see their taxes fall, on average, by $1,883.
• 25 million small business owners will receive an average tax cut of $3,001.

If Congress Does Not Act, Americans Will Pay Higher Taxes in 2005

If the tax cuts that expire after 2004 are not extended for 2005, taxes will increase for taxpayers who otherwise would benefit from these provisions.

• Lower income taxpayers will not receive $5.7 billion in relief from the expanded 10 percent rate.
• Taxpayers will not receive $8.9 billion in marriage penalty tax relief
• Families with children will not receive $13.2 billion in relief from the child tax credit. In 2005, the increased child credit, additional marriage penalty relief, and expanded 10 percent bracket will sunset, increasing the tax burden on a family of four earning $40,000 by $915.

93 million taxpayers would pay, on average, a tax increase of $565.

• 70 million women would see their taxes increase, on average, by $697
• 46 million married couples would pay, on average, an additional $960 in taxes
• 37 million families with children would incur an average tax increase of $954
• 8 million single women with children would see their taxes increase, on average, by $357
• 11 million elderly taxpayers would pay, on average, an additional $398 in taxes
• 23 million small business owners would incur tax increases averaging $831
• Nearly 2 million individuals and families who currently have no income tax liability would become subject to the income tax.
• President Bush's budget extends AMT relief through 2005. Without these changes, these taxpayers would pay an additional $23.2 billion in tax as a result of the AMT.

FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
JS-1183

Treasury Announces Actions Against AL-Haramain

The United States Attorney's Office for the District of Oregon announced a federal search warrant was executed yesterday against property purchased on behalf of the Al Haramain Islamic Foundation, Inc. in Ashland, Oregon.

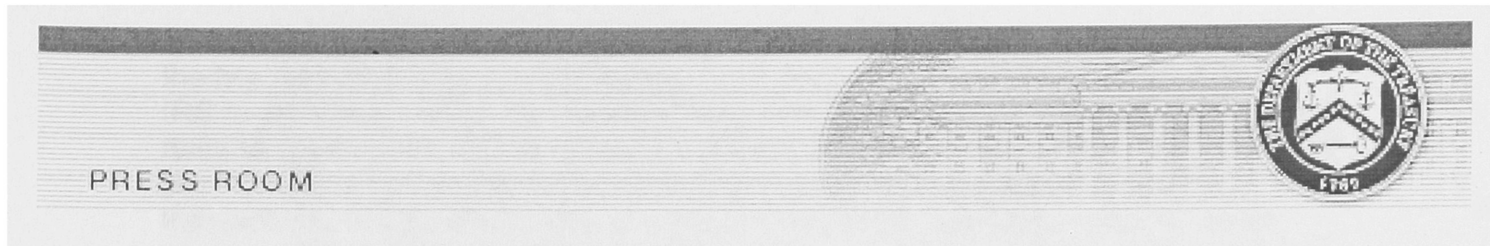
The search was led by agents of the Internal Revenue Service-CI as part of a joint Federal Bureau of Investigation (FBI) and Department of Homeland Security (DHS)/Immigration and Customs Enforcement investigation.

This search was conducted pursuant to a criminal investigation into possible violations of the Internal Revenue Code, the Money Laundering Control Act and the Bank Secrecy Act. The suspected crimes relate to possible violations of the currency reporting and tax return laws by two officers of the Ashland Oregon office of Al Haramain Foundation, Inc.

In a separate administrative action today, the Treasury's Office of Foreign Assets Control (OFAC) has blocked pending investigation accounts of the Al Haramain Foundation, Inc. to ensure the preservation of its assets pending further OFAC investigation.

The parent of the Oregon Al Haramain Islamic Foundation is headquartered in Saudi Arabia, and is one of that country's largest Non Governmental Organizations, with worldwide reach.

In March 2002, the United States Treasury and the Kingdom of Saudi Arabia jointly designated the Bosnian and Somalia Branches of Al Haramain as supporters of terrorism. In December 2003, the reconstituted branch of Al Haramain in Bosnia, Vazir, was also designated by both governments as a supporter of terrorism. In January 2004, the Kingdom of Saudi Arabia and the U.S. Department of the Treasury jointly designated four additional Al Haramain branches – Indonesia, Tanzania, Kenya and Pakistan – as being supporters of terrorism. The United Nations has adopted these Al Haramain designations and imposed an asset freeze, travel ban and arms embargo pursuant to United Nations Security Council Resolutions 1267/1390/1455.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
JS-1184

Bush Administration's Aggressive Actions to Combat Abusive Tax Shelters

The Bush Administration has taken aggressive action to address the abusive tax shelter problem, more so than in any period in recent memory. Tax shelters are being addressed effectively through ***increased disclosure*** by taxpayers and promoters, ***timely response*** by the Treasury Department and the IRS to transactions that are identified, and, ***where necessary***, ***targeted legislative*** changes to the substantive tax laws. The Administration's actions to carry out each of these principles have been focused, significant, and effective:

· The Administration is taking vigorous enforcement action against abusive tax shelters.
· The Administration has increased the disclosure of abusive tax shelters.
· The Administration is using its regulatory authority to shut down abusive tax shelters.
· The Administration's legislative proposals will:
- Shut down specific abusive tax shelters.
- Give the IRS important new tools and enhance its ability to combat abusive tax shelters.
- Enhance the IRS' effectiveness without compromising taxpayer protections.
· The Administration is reining in international tax abuses.

So-called "technical tax shelters" proliferated in the 1990s because taxpayers and promoters believed that taxpayers could enter into aggressive transactions with little risk of detection and with little risk of owing anything more than the tax due and interest even if caught. The Administration's approach to tax shelters is changing completely the risk-reward calculus for taxpayers considering an abusive transaction. The IRS' audits of the promoters of these tax shelters over the past three years have been unprecedented. Taxpayers and promoters no longer will be able to avoid detection. The Treasury Department and the IRS will take the steps necessary to shut down tax shelters – including appropriate enforcement action against taxpayers and promoters – as they are identified.

Beginning back in early 2002, the Administration proposed significant legislation to end the "hide-and-seek" tactics of promoters and taxpayers involved in these abusive transactions. In addition, the Administration is committed to providing the IRS with the resources and support needed to ensure that all taxpayers pay their fair share. The Administration's FY 2005 Budget includes an additional $300 million for IRS efforts to ensure compliance with the tax laws, and increases the total IRS budget by 4.8 percent – significantly above the average for non-defense, non-homeland security discretionary spending. The budget continues a three year trend of increasing resources for the IRS to improve taxpayer compliance and to target abusive transactions, while maintaining customer service to taxpayers.

Shutting down abusive transactions is not amenable to an easy, "one size fits all" solution. There simply is no "silver bullet" to the problem of tax shelters, and the Administration's actions reflect the comprehensive steps needed to effectively address this problem. Broad anti-abuse provisions, such as the proposed codification of the economic substance doctrine, may appear to be simple and attractive. They would do more, however, to burden careful taxpayers and practitioners – and the IRS – than stop abusive transactions. Complex rules would be needed to address the wide range of everyday business transactions that would

be affected by a broad, anti-abuse rule. But those regulations, in fact, would make the law less clear and more complex, and complex rules are more difficult for the IRS to administer fairly. At the same time, it is impossible for statutory or regulatory rules to cover every factual situation. A codified rule also would not stop those who are inclined to find economic substance and business purpose in virtually any transaction. It is far preferable to leave the economic substance doctrine to the courts – where it was originally conceived in the 1930s – which are better suited to applying the doctrine with flexibility. The judicial doctrine of economic substance requires an intensely factual inquiry, and these types of inquiries should be done by a court based on the actual facts of the case before it.

The specific steps taken by the Administration to address tax shelters are detailed below.

The Administration Is Taking Vigorous Enforcement Action Against Abusive Tax Shelters

Effective action against tax shelters requires effective tax administration. Over the past three years, the Treasury Department and the IRS have been working closely together to implement an effective strategy for dealing with abusive transactions. Although the actions described below relate to so-called "technical" tax shelters, the IRS also has an extensive program in place to address promoters of schemes and scams marketed primarily to individuals and small businesses, as well as the taxpayers who enter into those schemes and scams.

· **The IRS Is Implementing a Coordinated Strategy for Tax Shelters** – Commissioner Mark Everson is focused on organizing and maximizing the effectiveness of the IRS' efforts to combat tax shelters. John Klotsche, a former chairman of a major international law firm, has joined the IRS as a Senior Advisor to the Commissioner and has responsibility over the coordination of the IRS' efforts to combat tax shelters. The Commissioner and Senior Advisor Klotsche are working to coordinate efforts within the agency, with the Treasury Department, and with the Department of Justice.

· **The Treasury Department and the IRS Have Issued Proposed Ethical Rules and Opinion Standards for Tax Practitioners** – Many promoters claim that they can provide taxpayers with opinions that will protect against penalties even if a tax shelter is successfully challenged by the IRS. In December 2003, the Treasury Department and the IRS issued new proposed regulations that set out best practices for tax practitioners and provide minimum standards for tax opinions used to support tax shelters. Finalizing these rules is a high priority for the Treasury Department and the IRS.

· **The IRS Has Established Coordinated, Transaction-Specific Task Forces to Address Identified Tax Shelters** – Beginning in 2002, the IRS began using transaction-specific task forces to coordinate activities to shut down tax shelters. These task forces consist of attorneys from the IRS Operating Divisions, the IRS Office of Chief Counsel, the IRS' Office of Tax Shelter Analysis (OTSA), and the Treasury Department. These task forces allow the IRS to quickly develop and coordinate the legal response to a tax shelter.

· **The IRS Has Expanded Its Partnership with States to Combat Tax Shelters** – In 2003, the IRS entered into a nationwide partnership agreement with tax authorities in 40 states and the District of Columbia to share data and coordinate examination efforts to combat tax shelters. This agreement recently was expanded to now cover 45 states, the District of Columbia and New York City, and the IRS has started sharing leads on more than 20,000 taxpayers.

· **The IRS Has Initiated Over 130 Promoter Audits** – Since the beginning of 2001, the IRS has initiated over 130 promoter audits, including audits of accounting firms, law firms, insurance companies, brokerage companies, banks, and other boutique and mid-size promoters. These promoter audits will help ensure compliance with the promoter disclosure rules and will examine whether promoter penalties should be asserted against particular promoters.

· **The IRS Has Served Over 350 Administrative Summonses on Tax Shelter Promoters** – Since the beginning of 2002, the IRS has served over 350 administrative summonses to tax shelter promoters and has referred over 120 summonses to the Department of Justice for enforcement. The Department of Justice has commenced enforcement actions in court with respect to 67 of these summonses. Administrative summonses have been, and will continue to be, an important source of information for the IRS regarding promoter activities and compliance.

· **The IRS Has Sought Court Permission to Serve John Doe Summonses in Five Promoter Cases** – Since the beginning of 2002, the IRS has sought, as required by statute, court permission to serve "John Doe" summonses in 5 promoter cases. John Doe summonses are an important tool for identifying taxpayers who may have entered into potential tax shelters.

· **The IRS Has Encouraged Voluntary Disclosure** – In December 2001, the IRS began a disclosure initiative (Announcement 2002-2) to give taxpayers an incentive to disclose questionable transactions and other items that may have resulted in an underpayment of tax. In order to obtain penalty relief under the initiative, a taxpayer was required to disclose all relevant information about the transaction, including the identity of any promoter. The IRS has been using the information from the 1,689 disclosures received to identify new promoters and potential tax shelters for investigation and appropriate enforcement action.

· **The IRS Is Using a Mandatory IDR to Identify Listed Transactions for LMSB Cases** – Since April 2002, the IRS' Large and Midsize Business Division (LMSB) has been using a uniform information document request (IDR) in all of its audits. This mandatory IDR requests information regarding all "listed" transactions (i.e., specifically identified in published guidance as a tax avoidance transaction) reported by the taxpayer on its returns. The mandatory IDR will ensure that all LMSB taxpayers under audit disclose listed transactions.

· **The IRS Has Developed Mandatory Penalty Guidelines for Listed Transactions** – The IRS issued penalty guidelines in December 2001 requiring the development of accuracy-related penalties for listed transactions. These guidelines will help ensure that appropriate penalties are applied with respect to listed transactions.

· **The IRS Has Conducted Three Settlement Initiatives** – In November 2002, the IRS announced three settlement initiatives to resolve, on a basis that is fair, cases involving three widely-marketed tax shelters: the Section 302/318 "basis shift" transaction, the Section 351 contingent liability transaction, and the highly-leveraged corporate-owned life insurance (COLI) transaction. These initiatives have allowed the IRS to resolve a significant number of cases on a basis that is fair to the government and taxpayers. These initiatives permit the IRS to focus its resources on other tax shelters.

· **The IRS Has Revised Its Tax Accrual Workpaper Policy to Request These Documents From Taxpayers Who Engage in Listed Transactions** – Tax accrual workpapers normally are prepared by taxpayers and their independent auditors to evaluate the taxpayer's tax reserves for financial accounting purposes. Starting in 2002, the IRS changed its policy so that it now may request these workpapers from taxpayers who have engaged in listed transactions. This change in policy is a significant disincentive for taxpayers considering entering into a listed transaction.

· **The IRS Has Entered into an Agreement with a Major Professional Firm to Ensure Compliance with the Disclosure Rules** – As a result of the IRS' audits of promoters of technical tax shelters, one large professional firm has agreed to work with the IRS to ensure ongoing compliance with the registration and list maintenance provisions of the Internal Revenue Code and regulations. The IRS' agreement with this firm will ensure the highest standards of practice and future compliance with the law and regulations. The IRS expects to use this agreement as a model for agreements with other practitioners.

The Administration Has Increased Disclosure Of Abusive Tax Shelters

Taxpayers will be far less willing to engage in tax shelters if they believe that their transactions will be identified and that they will have to defend their transactions to the IRS and in the courts. The early disclosure of tax shelters also will allow the Treasury Department and the IRS to respond to abusive transactions before they spread throughout the market. Over the past two years the Administration has significantly overhauled rules requiring disclosure of abusive transactions by taxpayers and promoters. In addition, the Administration has proposed statutory changes that will further expand and strengthen the disclosure system. The Treasury Department originally announced these proposed statutory changes in March 2002, and the Administration remains committed to working with Congress to ensure that these important proposals are enacted into law.

· **Expanded and Simplified the Taxpayer Return Disclosure Regulations** – Temporary regulations issued in February 2000 required the disclosure of potentially questionable transactions. These rules, however, were limited to corporate taxpayers and were complex and subjective. The Treasury Department and the IRS finalized new disclosure regulations in February 2003 to increase disclosure and make the regulations easier to apply and administer. These new regulations contain straightforward, objective rules with no subjective exceptions. They apply to all taxpayers, including individuals, trusts, and partnerships.

Expanded and Simplified the Promoter List-Maintenance Regulations – Temporary regulations issued in February 2000 required promoters to maintain lists of taxpayers who participated in potentially questionable transactions. These rules were complex and subjective. The Treasury Department and the IRS finalized new list-maintenance regulations in February 2003 to broaden the list-maintenance requirements. These new regulations contain straightforward, objective rules that work with the new disclosure regulations to give the IRS multiple sources of information on a potential tax shelter. Coordinated rules for taxpayers and promoters will end the "conspiracy of silence" that made it more difficult for the IRS to identify and take action against tax shelters.

· **Issued Final Regulations for Promoter Registration of Certain Tax Shelters** – Temporary regulations issued in February 2000 required promoters to register certain tax shelters with the IRS. The Treasury Department and the IRS finalized the registration regulations in February 2003. When the Administration's proposal to amend the underlying statute is enacted into law, the Treasury Department and the IRS will issue new registration regulations to fully coordinate the three sets of disclosure rules: taxpayer return disclosure, promoter registration, and promoter list-maintenance.

· **Issued Final Penalty Regulations to Address Taxpayers Who Fail to Disclose Potential Tax Shelters** – In the absence of a specific penalty for the failure to disclosure a transaction on a return, some taxpayers were choosing to not disclose the transaction and to rely on an opinion to avoid any penalties if the transaction is successfully challenged by the IRS. In December 2003, the Treasury Department and the IRS issued final penalty regulations limiting the penalty defenses for taxpayers who fail to disclose potential tax shelters or positions based on advice that a regulation is invalid.

Proposed a New Schedule M-3 to Prioritize Book-Tax Differences – The Schedule M-1 that is part of the corporate income tax return requires taxpayers to identify differences between their taxable income and their financial, or book, income. The rules for disclosing these book-tax differences are unclear. The Treasury Department and the IRS recently proposed a new corporate income tax form to make book-tax differences more transparent. The new Schedule M-3 will allow the IRS to more quickly identify differences that may have resulted from an aggressive tax position or a potential tax shelter. Better disclosure of book-tax differences will allow the IRS to focus its resources more efficiently on potentially significant, emerging issues.

Proposed Legislation to Fully Coordinate the Disclosure Rules – Disclosure works best when the IRS has multiple sources of information about a tax shelter

that form a complete web of disclosure. Existing statutes do not permit uniform and consistent rules. The Administration's FY 2005 Budget again proposes to change the promoter registration and list-maintenance statutes to permit uniform and consistent taxpayer and promoter disclosure rules.

· **Proposed Legislation to Impose Meaningful Penalties on Taxpayers who Fail to Disclose** – A taxpayer currently faces no penalty for the failure to disclose a potentially abusive transaction on a return. Only Congress may provide for a nondisclosure penalty. The Administration's FY 2005 Budget again proposes penalties of up to $200,000 for taxpayers who fail to disclose potential tax shelters. In addition, public companies would be required to disclose in their SEC filings any penalties for failing to disclose a transaction that the Treasury Department and the IRS have identified as a "tax avoidance" (or "listed") transaction.

· **Proposed Legislation to Increase Penalties on Promoters who Fail to Register a Transaction** – The Administration's FY 2005 Budget again proposes to increase the existing penalties for a promoter's failure to register a transaction with the IRS. Along with the Administration's proposal to broaden the reach of the promoter registration statute, this proposal will impose meaningful penalties on promoters who fail to register a potential tax shelter.

· **Proposed Legislation to Increase Penalties on Promoters who Fail to Maintain Lists of Taxpayers who Have Engaged in Potential Tax Shelters** – Existing penalties on promoters who fail to maintain lists of participating taxpayers are insufficient. The Administration's FY 2005 Budget again proposes significant penalties of $10,000 per day on promoters for the failure to provide the IRS with lists of taxpayers who have engaged in potential tax shelters.

The Administration Is Using Its Regulatory Authority To Shut Down Abusive Tax Shelters

The Treasury Department and the IRS have used the authority under section 6011 to identify in published guidance (or "list") specific "tax avoidance" transactions. The recently revised disclosure and list-maintenance rules impose stringent disclosure requirements on taxpayers and promoters for listed transactions. These listing notices also make clear to taxpayers and promoters that the Treasury Department and the IRS are aware of these abusive transactions and that the IRS is committed to taking appropriate enforcement action against participating taxpayers and promoters. Listing notices have been one of the most effective actions taken over the past three years to stop tax shelters. Over the past three years, the Administration has listed the following transactions:

· **Abusive Foreign Tax Credit Transactions** – These transactions involve a domestic corporation's transitory ownership of a foreign target corporation when, pursuant to a prearranged plan, the domestic corporation acquires the stock of the target corporation and then all or substantially all of the target corporation's assets are sold in a transaction that gives rise to foreign tax without a corresponding inclusion of income for U.S. tax purposes. The Treasury Department and the IRS issued Notice 2004-20 to shut down these transactions. The Treasury Department and the IRS at the same time also issued Notice 2004-19, which details the legislative and regulatory approaches that the Treasury Department and the IRS are using to address other abusive foreign tax credit transactions.

· **Abusive Excess Life Insurance in Defined Benefit Pension Plans** – These arrangements involve specially designed life insurance policies intended primarily to benefit highly-compensated employees through a retirement plan. The Treasury Department and the IRS issued Rev. Rul. 2004-20 to shut down abusive excess life insurance arrangements.

· **Abusive S Corporation ESOP Arrangements** – These arrangements are intended to assist companies in avoiding tax rules designed to protect rank-and file participants in employee stock ownership plans ("ESOPs"). The Treasury Department and the IRS issued Rev. Rul. 2003-6 and Rev. Rul. 2004-4 to stop these abuses and protect rank-and-file participants in S corporation ESOPs.

· **Abusive Roth IRA Transactions –** These arrangements involve the contribution of property to an IRA through a transaction that disguises the value of the contribution to circumvent Roth IRA contribution limits. The Treasury Department and the IRS issued Notice 2004-8 to stop abusive structures designed to avoid the contribution limits that apply to Roth IRAs.

· **Abusive Offsetting Foreign Currency Option Contract Transactions –** These transactions involve two pairs of offsetting foreign currency options. Two of the offsetting options are assigned to a charity, and the taxpayer claims an immediate loss on one option without recognizing the offsetting gain on the other. The Treasury Department and the IRS issued Notice 2003-81 to shut down these transactions.

· **Abusive Contested Liability Transactions** – These transactions involve the purported establishment of trusts to accelerate deductions for liabilities that a taxpayer is contesting under section 461(f). The trusts, however, do not comply with the requirements of that section because the taxpayer either retains control over the trust assets or transferred its own stock or the stock or note of a related party. The Treasury Department and the IRS issued Notice 2003-77 to prevent the use of trusts to accelerate deductions.

· **Abusive Stripping Transactions –** These transactions improperly separate income from related deductions. Some of these transactions, for example, are structured to have a tax-indifferent party realize the taxable income while the taxpayer claims deductions related to that income, such as depreciation or rental expenses. The Treasury Department and the IRS issued Notice 2003-55 to shut down these transactions.

· **Abusive Option Sales to Family Limited Partnerships** – These arrangements involve the purported sale of compensatory stock options to a limited partnership owned by the taxpayer's family members to avoid income and employment taxes on the exercise of the options. The Treasury Department and the IRS issued Notice 2003-47 to shut down these transactions.

· **Abusive Welfare Benefit Funds** – These transactions are designed to avoid the applicable deduction limits on contributions to welfare benefit funds. Taxpayers claim that the benefits are being provided under a collective bargaining agreement. The Treasury Department and the IRS issued Notice 2003-24 stop these abuses and further addressed these transactions in final regulations issued July 2003.

· **Abusive Offshore Deferred Compensation Arrangements** – These transactions are designed to avoid income and employment taxes by utilizing a purported lease of the right to a taxpayer's services in the United States through a foreign leasing company. The proceeds of the leasing arrangement are transferred to an offshore trust maintained on behalf of the taxpayer. The Treasury Department and the IRS issued Notice 2003-22 to shut down these abusive offshore employee leasing arrangements.

· **Abusive Producer Owned Reinsurance Company ("PORC") Arrangements** – These insurance arrangements involve a foreign corporation established to reinsure the policies sold by a taxpayer in connection with the sale of products or services. The taxpayers utilize various exemptions of income for insurance companies to divert portions of the premiums paid to the PORC and pay little or no tax on the diverted funds. The Treasury Department and the IRS issued Notice 2002-70 to shut down these arrangements.

· **Abusive Lease-In/Lease-Out ("LILO") Transactions** – LILOs involve a lease of property from a tax-indifferent party (e.g., a foreign party or a tax-exempt party), and a simultaneous lease of the same property back to the tax-indifferent party to generate substantial deductions of the lease payments. The Treasury Department and IRS issued Rev. Rul. 2002-69 to supersede earlier guidance issued to shut down these transactions.

· **Abusive Partnership Straddle Tax ("Eliminator") Transactions** – These

transactions involve the use of a straddle, a tiered partnership structure, a transitory partner, and the partnership allocation rules to generate purported permanent non-economic tax losses for the taxpayer. The Treasury Department and the IRS issued Notice 2002-50 to shut down these transactions.

· **Abusive Passthrough Entity Straddle Transactions** – These transactions involve the use of a straddle, one or more transitory S corporation shareholders, and the rules of subchapter S to allow a taxpayer to claim an immediate loss while deferring an offsetting gain. The Treasury Department and the IRS issued Notice 2002-65 to shut down these transactions.

· **Abusive Common Trust Fund Straddle Transactions** – These transactions involve the use of a common trust fund that invests in economically offsetting gain and loss positions in foreign currencies and allocates the gain to one or more tax-indifferent parties and the losses to the taxpayer. The Treasury Department and the IRS issued Notice 2003-54 to shut down these transactions.

· **Abusive 401(k) Accelerated Deductions** – These transactions involve claims by employers of accelerated deductions for contributions to retirement plans on compensation expected to be earned by participants in future years. The Treasury Department and the IRS issued Rev. Rul. 2002-46 to expand earlier guidance identifying these listed transactions.

· **Abusive Notional Principal Contracts or Contingent Swaps** – These transactions involve the use of a notional principal contract to claim current deductions for periodic payments made by a taxpayer while disregarding the accrual of a right to receive offsetting payments in the future. The Treasury Department and the IRS issued Notice 2002-35 to stop these abuses.

· **Abusive Inflated Basis ("CARDS") Transactions** – These transactions involve the use of a loan assumption agreement to claim an inflated basis in assets. The assets are sold for fair market value and the taxpayer claims a significant loss, arguing that the entire principal amount of the loan is included in taxpayer's basis. The Treasury Department and the IRS issued Notice 2002-21 to shut down these transactions.

· **Abusive Section 302/318 "Basis Shift" Transactions** – These transactions involve an abuse of the attribution rules to increase the basis of the stock held by the taxpayer through a redemption of stock held by a tax-indifferent party (typically, a foreign entity). The taxpayer claims a loss on the sale of its stock based on its position that the basis of the redeemed stock is added to the basis of stock the taxpayer sold. The Treasury Department and the IRS issued Notice 2001-45 to shut down these transactions.

Promoters of tax shelters often attempt to take advantage of highly technical tax rules to obtain tax benefits not intended by Congress. The Administration is using its regulatory authority whenever appropriate to stop abusive transactions and eliminate potential opportunities for abuse. Administrative actions taken over the past three years include:

· **Issued Final Regulations to Stop Abusive Split-Dollar Life Insurance Arrangements** – "Split-dollar life insurance arrangements" have been used to provide some corporate executives with tax-free compensation and to make tax-free gifts among family members. In September 2003, the Treasury Department and the IRS issued final regulations that shut down the use of these arrangements.

· **Issued Notice to Stop Abusive "Reverse Split-Dollar Life Insurance Arrangements"** – "Reverse split-dollar life insurance arrangements" were being marketed as a means to avoid gift and estate taxes on wealth transfers to family members. The Treasury Department and the IRS issued Notice 2002-59 to shut down these arrangements.

· **Issued Final Regulations to Stop Abusive Hedged Deferred Compensation**

Liability Arrangements – These transactions were being used to claim favorable hedging income tax treatment with regard to certain deferred compensation arrangements. In March 2002, the Treasury Department and the IRS issued final regulations to prevent these claimed tax benefits.

· **Issued Revenue Rulings to Stop "Double-dip" Health Benefit Deduction Schemes** – Promoters had been marketing schemes that purport to exclude health insurance premiums from an employee's income twice – i.e., once when paid by a reduction in salary and a second time when the amount of the salary reduction was reimbursed. The Treasury Department and the IRS issued Rev. Rul. 2002-3 and Rev. Rul. 2002-80 to shut down these arrangements, which often were not disclosed to the employees.

· **Issued Final Regulations to Stop Abusive Deferred Compensation Schemes for Nonprofit Executives** – Some nonprofit organizations offered steeply discounted "options" to executives to purchase mutual funds. These arrangements effectively gave the executives cash compensation that could be claimed at any time, even though the compensation was purported to be not taxable until claimed. In July 2003, the Treasury and IRS issued final regulations that made these options and similar arrangements currently taxable.

· **Issued Revenue Ruling to Stop Potential Abuses Involving Donations of Patents** – Some taxpayers had claimed deductions for contributions of patents that far exceed the actual value of the patent to the recipient public charity. The Treasury Department and the IRS issued Rev. Rul. 2003-28 to clarify that certain transfers of rights in a patent do not give rise to a charitable contribution deduction. The Administration's FY 2005 Budget also proposes to limit further a taxpayer's ability to claim a deduction for the contribution of a patent or other intellectual property.

· **Issued Revenue Ruling on Purported Insurance Companies Used to Reduce Tax on Investment Income** – Some taxpayers had created purported insurance companies in foreign jurisdictions to shield investment income from U.S. tax. The Treasury Department and the IRS issued Rev. Rul. 2003-34 to notify taxpayers that the IRS will challenge certain off-shore insurance company arrangements used to reduce tax on investment income. The Administration's FY 2005 Budget proposes to curtail the abuse of these insurance company arrangements.

· **Issued Temporary Regulations to Stop "Son of BOSS" Transactions** – Notice 2000-44 identified the so-called "Son of BOSS" transaction as a listed transaction. Some promoters continued to market this tax shelter, and some taxpayers were still entering into these transactions. In June 2003, the Treasury Department and the IRS issued temporary regulations under section 358(h) to stop these "Son of BOSS" transactions.

· **Issued Revenue Ruling to Stop Tax Shelters Involving Variable Life Insurance and Annuity Contracts** – Some taxpayers had entered into variable life insurance or annuity contract arrangements to avoid current tax on income and gain from the underlying assets even though the taxpayers retained effective ownership over these assets. The Treasury Department and the IRS issued Rev. Rul. 2003-92 to stop these arrangements.

· **Issued Notice to Stop the Use of Stapled Stock Structures to Artificially Increase Foreign Tax Credits** – Congress enacted section 269B in 1984 to address the potential for tax avoidance in certain structured transactions involving stock of two corporations (one foreign and one domestic) that cannot be transferred separately due to contractual restrictions. Since then, however, taxpayers had sought to use the rules of section 269B to their advantage by creating stapled stock structures to artificially increase their foreign tax credits by manipulating the allocation and apportionment of expenses such as interest. The Treasury Department and the IRS issued Notice 2003-50 to halt these transactions by announcing an immediately effective, targeted change to the rules of section 269B, and by reminding taxpayers of the potential applicability of existing principles of law, such as the substance-over-form doctrine, to these transactions.

· **Proposed New Information Reporting Requirements on U.S. Persons that Own Certain Foreign Entities** – The Treasury Department and the IRS issued Announcement 2004-4 to propose new Form 8858. This form will require information reporting by U.S. persons that own foreign disregarded entities. This information reporting requirement will provide a means for the IRS to identify potential compliance issues efficiently in an area in which there currently is inadequate information reporting and will allow the IRS to better focus its audit resources.

· **Issued Temporary Regulations to Require Information Reporting to Shareholders on Corporate Inversion Transactions** – Corporate inversion transactions generally result in the shareholders of the inverting company recognizing gain on their stock as a result of the transaction. The Treasury Department and the IRS issued regulations in 2002 that require inverting corporations to provide information reporting on these transactions to ensure that the shareholders accurately report the gain recognized as a result of an inversion.

· **Issued Final Regulations to Eliminate Inappropriate Benefits from Domestic Reverse Hybrids** – The Treasury Department and the IRS issued final regulations in 2002 to eliminate the benefits of a structure involving a hybrid entity established in the United States that makes payments to a parent company established in a country with whom the U.S. has a tax treaty that was designed to give rise to a deduction in the United States and exemption from tax in both the United States and the treaty country.

Issued Regulations to Clarify the Treatment of Stock-Based Compensation in Cost Sharing Arrangements – The Treasury Department and the IRS issued regulations in 2003 on the tax treatment of stock-based compensation under the related party transfer pricing rules governing qualified cost sharing arrangements. These regulations are aimed at ensuring that the rules governing qualified cost sharing arrangements for the joint development of intangible assets cannot be used to facilitate the migration of intangibles outside the United States for less than arm's length compensation.

The Administration's Legislative Proposals Will Shut Down Specific Abusive Tax Shelters

The Administration's FY 2005 Budget builds on earlier Administration legislative proposals to strengthen the disclosure rules and on the information gathered through IRS compliance programs. The new legislative proposals close loopholes and target identified tax shelters and abusive practices. As other abusive transactions are identified, the IRS will challenge the transactions in audits, and the Treasury Department and the IRS will work with Congress to enact any legislation necessary to address the transactions.

· **Proposed Legislation to Stop Abusive Leasing Transactions with Tax-Indifferent Parties** – Taxpayers increasingly have used purported leasing transactions, often referred to as SILO transactions, to "acquire" significant tax benefits from a tax-indifferent party, such as a municipal transit authority or foreign government, in exchange for a modest fee. These transactions do not involve any useful economic activity, such as the acquisition or financing of business assets. The Administration's FY 2005 Budget proposes to sharply limit the tax benefits that a taxpayer can claim in these transactions.

· **Proposed Legislation to Eliminate Abusive Transactions Involving Foreign Tax Credits** – Current law provides taxpayers with a credit for certain foreign taxes in order to eliminate the double taxation of foreign income (i.e., taxation by both the United States and the country where the income is earned). Taxpayers have structured transactions in an attempt to use foreign tax credits not to eliminate double taxation, but inappropriately to reduce their U.S. tax liability on unrelated foreign income. The Administration's FY 2005 Budget proposes to deny foreign tax credits for foreign withholding taxes imposed on income if the underlying property generating the income was not held for a specified minimum period of time. In addition, the Administration's proposals would provide the Treasury Department with regulatory authority to prevent transactions that inappropriately separate

foreign taxes from the related foreign income to take advantage of the foreign tax credit rules where there is no real risk of double taxation.

· **Proposed Legislation to Stop Abusive Income-Separation Transactions** – Some taxpayers continue to engage in transactions that separate the periodic income steam from an underlying income-producing asset in order to generate an immediate tax loss for one taxpayer and the conversion of current taxable income into deferred capital gain for another. Although the Tax Code prohibits these transactions for bonds and preferred stock, taxpayers have been engaging in essentially identical transactions using similar assets, such as shares in a money-market mutual fund. The Administration's FY 2005 Budget again proposes to treat an income-separation transaction as a secured borrowing, not a separation of ownership. Debt characterization will ensure that the tax treatment of the transaction clearly reflects income.

· **Proposed Legislation to Prevent the Misuse of Tax-Exempt Casualty Insurance Companies** – Certain small casualty insurance companies are not subject to federal income tax. Some taxpayers are abusing this rule by creating insurance companies, claiming tax-exempt status, and improperly accumulating investment income tax-free. The Administration's FY 2005 Budget proposes to prevent taxpayers from using this targeted exemption to inappropriately avoid tax on investment income.

· **Proposed Legislation to Tighten the Deduction Limitation for Interest Paid to Related Parties** – Current law denies a deduction for certain interest paid by a corporation to a related party to the extent the corporation's net interest expenses exceed 50 percent of its taxable income (computed with certain adjustments). This limitation only applies if the corporation's debt-equity ratio exceeds 1.5 to 1.0. In order to address the opportunities available under current law to inappropriately reduce taxes on U.S. operations through the use of foreign related party debt, the Administration's FY 2005 Budget proposes to tighten the limitation for related party interest expense.

· **Proposed Legislation to Prevent Avoidance of U.S. Tax on Foreign Earnings Invested in U.S. Property** – Under current law, U.S. shareholders of a controlled foreign corporation must include in income their pro rata share of earnings of the corporation that are invested in certain U.S. property. Deposits with banks are excluded from the definition of U.S. property subject to this rule, however, so that taxpayers operating through foreign subsidiaries are not discouraged from using the U.S. banking system. This exception has been interpreted in a manner inconsistent with the underlying policy. For example, certificates of deposit have been issued by a U.S. affiliate in a transaction structured to take advantage of the bank exception. Under the proposal contained in the Administration's FY 2005 Budget, the exception for deposits with persons carrying on the banking business would be modified to eliminate this potential for abuse.

· **Proposed Legislation to Modify Tax Rules for Individuals Who Give Up U.S. Citizenship or Green Card Status** – If an individual gives up U.S. citizenship, or terminates long-term U.S. residency, with a principal purpose of avoiding U.S. tax, the individual is subject to an alternative tax regime for 10 years. The Administration's FY 2005 Budget proposes changes designed to improve compliance with the expatriation rules.

· **Proposed Legislation to Stop Abuses by Requiring Charitable Deductions to Reflect Accurately the Value of the Donation** – Some taxpayers are abusing the laws designed to support charities by claiming deductions for contributions of certain property (e.g., patents, intellectual property, and motor vehicles) that far exceed the value of the property donated. The Administration's FY 2005 Budget proposes to impose additional appraisal requirements and, in the case of patents and certain other intellectual property, limit the amount that can be deducted to match the value of the donation.

· **Proposed Legislation to Stop Abuses of Section 529 College Savings Plans** – Section 529 college savings plans involve a number of issues that are not clearly answered by current law. As a result, these savings plans could be abused to

avoid transfer taxes. The Administration's FY 2005 Budget proposes to clarify the rules to prevent abuse and to make the applicable rules more equitable. The Administration's proposal would further encourage savings for college expenses through these increasingly popular plans.

The Administration's Legislative Proposals Will Give the IRS Important Tools and Enhance Its Ability To Combat Abusive Tax Shelters

The Administration's FY 2005 Budget contains a number of important legislative proposals that will allow the IRS to deal more effectively with abusive tax shelters. Many of these proposals are designed to end practices used by some taxpayers and promoters to impede or delay examination. Taxpayers who are willing to enter into abusive transactions and promoters who are willing to recommend abusive transactions should be willing to disclose these transactions and subject them to IRS scrutiny.

· **Proposed Legislation to Permit Injunction Actions against Promoters** – Some promoters repeatedly disregard their legal obligations, including the registration and list-maintenance requirements. The Administration's FY 2005 Budget again proposes to confirm the Government's authority to enjoin the most egregious promoters of tax shelters, as it is doing currently with promoters of tax scams directed primarily at individuals and small businesses.

· **Proposed Legislation to Impose a New Penalty for the Failure to Report an Interest in a Foreign Financial Account** – Individual taxpayers are required to disclose on their tax returns interests in a foreign financial account, such as a bank account. The Administration's FY 2005 Budget again proposes a new civil penalty for the failure to disclose foreign financial accounts, which often are used in tax avoidance transactions.

· **Proposed Legislation to Stop Taxpayers and Promoters from Using the Federal Practitioner Privilege to Delay Disclosing Potential Tax Shelters** – Some practitioners and non-corporate taxpayers are claiming the statutory practitioner-client privilege in order to delay the IRS' efforts to identify and examine potential tax shelters. The Administration's FY 2005 Budget again proposes to eliminate the privilege with respect to tax shelters and proposes to confirm that the identity of any person that a promoter is required to identify to the IRS is not privileged.

Proposed Legislation to Eliminate the Incentive for Taxpayers and Promoters to Delay Disclosing Potential Tax Shelters – Some taxpayers and practitioners are delaying the IRS' efforts to identify and examine potential tax shelters in order to run out the statute of limitations. The Administration's FY 2005 Budget proposes to extend the statute of limitations for potential tax shelters that a taxpayer fails to disclose until the transaction is disclosed to the IRS by either the taxpayer or the promoter. The IRS, with the assistance of the Department of Justice, is challenging inappropriate claims of privilege in the courts where necessary.

· **Proposed Legislation to Increase the Penalties for False or Fraudulent Statements Made to Promote Abusive Tax Avoidance Transactions** – Existing penalties are insufficient to deter some promoters from making false or fraudulent statements regarding the claimed benefits of a potential tax shelters. The Administration's FY 2005 Budget proposes to increase significantly the penalty for making false or fraudulent statements to up to 50 percent of the fees earned.

The Administration's Legislative Proposals Will Enhance The IRS' Effectiveness Without Compromising Taxpayer Protections

The Administration is committed to exploring ways in which the IRS can work more effectively without compromising taxpayer protections. By working more effectively, the IRS can devote more resources to a range of priorities, including abusive transactions. Americans must be confident that the IRS is taking all appropriate actions to ensure that all taxpayers are paying their fair share.

· **Proposed Legislation to Expand the Use of Electronic Filing** – The IRS has taken a number of steps to expand the availability and increase the use of electronic filing, which reduces costs and speeds processing for both taxpayers and the Government. The Administration's FY 2005 Budget again proposes to extend the April 15 filing date to April 30 for returns that are filed electronically, provided that any tax due also is paid electronically. This proposal would encourage more taxpayers to file electronically and allow the IRS to process more returns and payments efficiently.

· **Proposed Legislation to Permit Private Collection Agencies to Support the IRS' Collection Efforts** – The IRS' resource and collection priorities do not permit the IRS to continually pursue all outstanding tax liabilities. Many taxpayers are aware of their outstanding tax liabilities but have failed to pay them, and the IRS cannot continuously pursue each taxpayer with an outstanding liability. The Administration's FY 2005 Budget again proposes to allow private collection agencies, or PCAs, to support the IRS' collection efforts in specific, limited ways. The proposal would enable the government to reach these taxpayers to obtain payment while allowing the IRS to focus its own enforcement resources on more complex cases and issues. PCAs would not have any enforcement power and would be carefully monitored to ensure that taxpayer rights are carefully protected.

· **Proposed Legislation to Curb Frivolous Returns and Submissions** – Some taxpayers are abusing taxpayer protections, such as the collection due process procedures, by making frivolous arguments to in order to delay or impede tax administration. The Administration's FY 2005 Budget again proposes to increase the penalty for frivolous returns and allow the penalty to be applied to frivolous submissions that are not withdrawn after IRS request. The IRS would be permitted to disregard non-return frivolous submissions that are not withdrawn.

· **Proposed Legislation to Terminate Installment Agreements if Taxpayers Fail to File Returns or Make Tax Deposits** – The IRS cannot terminate an installment agreement even if a taxpayer fails to file required returns or fails to make required federal tax deposits. The Administration's FY 2005 Budget again proposes to permit the IRS to terminate an installment agreement in these situations.

· **Proposed Legislation to Streamline the Handling of Collection Due Process Cases** – The rules regarding the proper court to review a collection due process case are unnecessarily complicated and have been used by some taxpayers to delay tax administration. The Administration's FY 2005 Budget again proposes to consolidate jurisdiction over collection due process cases in the Tax Court.

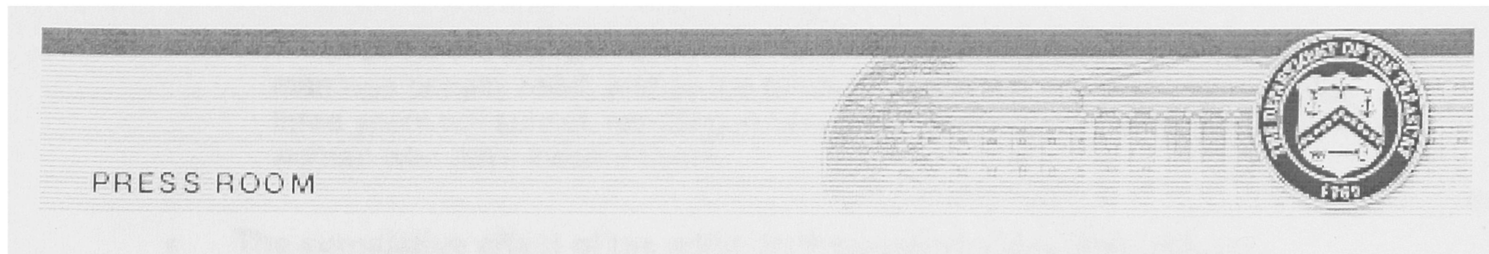
· **Proposed Legislation to Improve Procedures for Taxpayers Seeking to Resolve Their Tax Liabilities** – The IRS must be able to work quickly with taxpayers who are seeking to resolve their tax liabilities in good faith. The Administration's FY 2005 Budget again proposes to permit the IRS to enter into installment agreements that do not guarantee full payment of a liability over the life of the agreement. This will permit the IRS to work with a broader range of taxpayers who desire to resolve their tax liabilities. The Administration's FY 2005 Budget also again proposes to expedite the review process for accepted offers-in-compromise.

The Administration Is Reining In International Tax Abuses

International tax abuses are particularly difficult to address, and the Administration is using all available tools to curtail abusive transactions and practices in this area.

· **Significantly Expanded Network of Bilateral Tax Information Exchange Relationships** – In the last two years, the United States has negotiated and concluded important new tax information exchange agreements with nine significant offshore financial centers, including The Bahamas, the British Virgin Islands, and the Cayman Islands. Each of these agreements reflects the international standards for tax information exchange that the United States has been a leader in establishing, and in each case the agreement is the first such agreement entered into by the offshore financial center with any country.

· **Prevented Tax Avoidance on Lump Sum Pension Distributions** – The new 2003 income tax treaty with the United Kingdom eliminated an abuse under which a person would establish transitory residence in the United Kingdom prior to receiving from a U.S. pension fund a lump sum distribution that otherwise would be taxable in the United States in order to claim tax exemption on the distribution in both the United States and the United Kingdom.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 20, 2004
JS-1185

President Bush Urges Congress to Make Tax Cuts Permanent

Today's Presidential Action

« President Bush today called on Congress to make his tax cuts permanent and discussed with taxpayers his plan to create jobs in America and to continue to grow and strengthen the economy.

« **New figures released today by the Treasury Department demonstrate the real benefits of the President¡¦s tax relief for all Americans**.

- Last July and August when tax relief checks went out, families with children received up to $400 per child ¡V in all, 24 million families received tax relief totaling $14 billion.
- The 2003 tax relief will also be felt this spring, as the Treasury Department estimates that Americans will receive an extra $50 billion in higher refunds and lower tax payments for the 2003 tax year when they file their taxes on April 15th.
- For the 2004 tax year, 111 million families will save an average of $1,586 because of the tax relief, a total of $176 billion in additional tax relief.

The President¡¦s Tax Relief is Working

« **America¡¦s economy is strong and getting stronger**. More Americans than ever own their homes. More businesses are investing. Indicators of manufacturing activity are the highest in the last two decades, and economic growth in the second half of 2003 was the highest in almost 20 years. Stock market wealth has increased by more than $4 trillion over the past 12 months, and more than 365,000 jobs have been added in the last five months. Because of the continuing effects of President Bush¡¦s tax relief, workers will continue to keep more of what they earn in the future, and small businesses will be better able to invest and grow. The President¡¦s policies are helping to put the economy on a path to sustained growth and job creation, but we cannot rest until every American who wants to work can find a job.

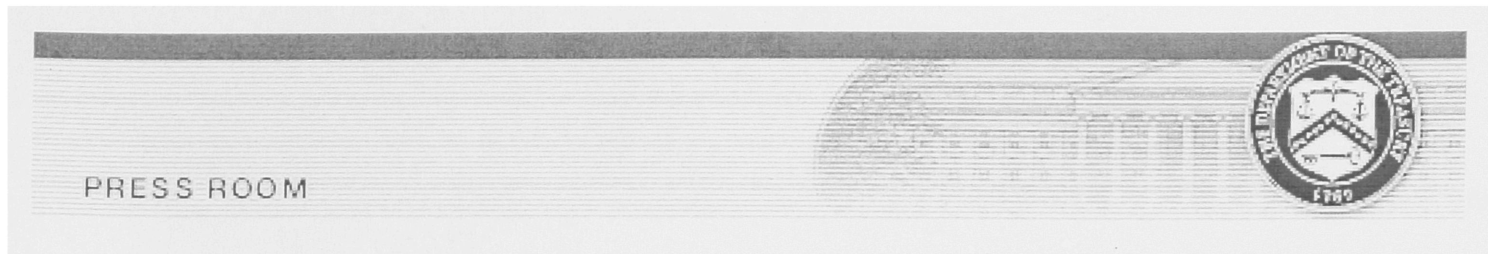
« **Over the past three years, President Bush has proposed and signed into law three separate tax relief measures, resulting in significant tax relief for millions of American families and businesses**. Failure to extend the President¡¦s tax cuts permanently would dramatically increase the burden on American taxpayers in future years. For example:

- In 2005, the increased child credit, additional marriage penalty relief, and expanded 10-percent bracket will shrink, increasing the tax burden on a family of four earning $40,000 by $915;
- In 2006, allowable small business expensing will shrink from $100,000 to just $25,000, increasing the cost of capital investments for America¡¦s small businesses;
- In 2009, the top tax rate on dividends will increase from 15 to 35 percent, while the tax on capital gains will climb from 15 to 20 percent, raising the tax burden on retirees and families investing for their future; and

- In 2011, the tax rate relief, new 10-percent tax bracket, death tax repeal, marriage penalty relief, and all the remaining tax relief enacted over the past three years will sunset, resulting in tax increases for every American man or woman who pays income taxes.

« **The cumulative effect of tax relief on the economy has been strong, laying the groundwork for increased economic growth and job creation. According to the Treasury Department, by the last quarter of 2003, the tax relief signed by President Bush had**:

- Reduced the unemployment rate by nearly 1 percentage point below where it would have been otherwise;
- Increased the jobs available to Americans by as many as 2 million; and
- Increased real GDP by as much as 3 percent.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 20, 2004
JS-1186

U.S. Treasury Official Visits Miami to Promote Financial Education and Launch Spanish Language Financial Education Resource Guide

The Department of the Treasury today announced that Kristin Smith, Director of the Office of Financial Education (OFE), is visiting Miami to promote financial education within the Hispanic community.

While in Miami, Smith will present an honorary certificate of recognition to the Greater Miami Prosperity Campaign for its successes in providing financial education to the community. In addition, Smith will launch the Spanish language version of the OFE's online Federal Financial Education Resource Directory, Directorio Federal de Educación Financiera, during the "Women & Money" Hispanic Financial Literacy Conference sponsored by the Women's Bureau of the Department of Labor at Miami Dade College.

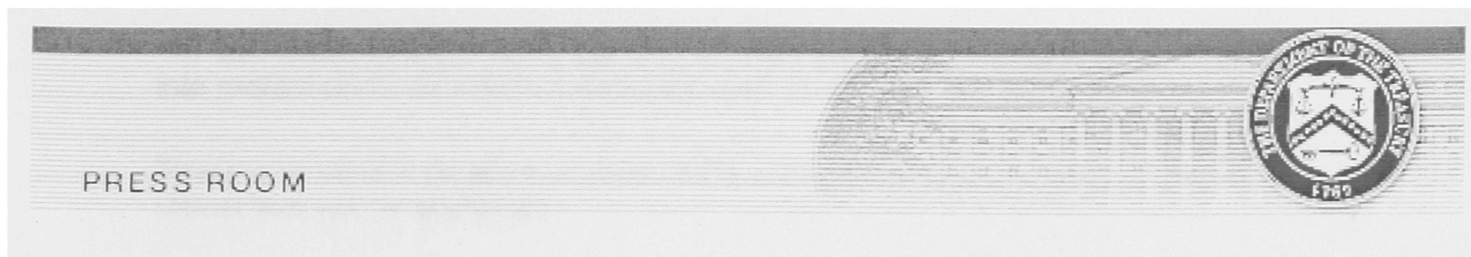
"Treasury's Office of Financial Education helps Americans access financial education programs to obtain the knowledge and skills they need to make informed financial choices throughout their lives." said Office of Financial Education Director Kristin H. Smith. "To enhance financial literacy in America, we highlight effective financial education programs across the country to increase the program's visibility within the community and try to make it easier for individuals to utilize existing resources."

The Greater Miami Prosperity Campaign's goals are to increase the number of workers in Miami-Dade County claiming the refundable federal Earned Income Tax Credit in the upcoming tax season, to promote financial education, and to enhance these workers' ability to build assets by linking them to financial institutions and asset development programs.

The Directorio Federal de Educación Financiera will provide an estimated 29 million U.S. residents who speak Spanish at home with access to the many financial education resources available within the federal government. The guide includes information on fifteen separate resources and programs available in Spanish, catalogued by subject area, program name, and sponsoring organization. This information can also be used to assist organizations that implement financial education initiatives within the Hispanic community.

The Spanish-language directory is available through the OFE's website at www.treasury.gov/financialeducation.

The Department of the Treasury's Office of Financial Education was established in May 2002. The OFE is responsible for focusing the Department's financial education policymaking, and for ensuring coordination on financial education within the Department and all of its bureaus. The OFE serves to provide the Department of the Treasury with expertise on the many complex and interdisciplinary issues involved in financial education, and is able to tap into the Department's wide base of expertise on finance. The OFE also supports the efforts of the Financial Literacy and Education Commission, a group chaired by the Secretary of Treasury and composed of representatives from 20 federal departments, agencies, and commissions, which works to improve financial literacy and education for people throughout the United States.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 23, 2004
JS-1188

Treasury Secretary John W. Snow
Credit Union National Association (CUNA)
Government Affairs Conference
Washington, DC

Thank you, Dan, and thank you all for having me here today.

It's always a pleasure to see Dan Mica… he is in a lot of the meetings I have with members of the financial community, and I want you to know that he does a very fine job representing you, the CUNA membership.

I enjoy having Dan in those meetings for a lot of the same reasons that I enjoyed coming to this meeting last year, and again today – and that has to do with the heart of the credit union community.

You are an extremely powerful group – in terms of dollars and influence – but you also have a lot of heart. You're in the financial world to do good as well as to do business… your motto of "not for charity, not for profit, but for service" rings true, throughout your ranks. And it makes you a pleasure to work with.

When I came to this meeting last year, I was very new to my job. The President was promoting his Jobs and Growth Tax Cut plan, and I was eager to help him out.

Because I know that tax cuts work, and I knew that our recovering economy needed that kind of stimulus.

The President had inherited an economy that was in decline… one that was then battered by terrorist attacks and revelations of corporate corruption dating back to the 1990s.

I'm pleased to report to you, this year, that those tax cuts that the President and I agreed were necessary – and which the Congress thankfully passed – did work, indeed.

Homeownership is up, unemployment is heading down, and GDP growth has been strong.

The President's tax cuts provided the stimulus that was necessary to turn our economic ship around… and they are now encouraging and allowing for the economic growth that is continuing into the future.

- Economic growth in the second half of 2003 was the fastest since 1984;
- New home construction was the highest in almost 20 years;
- Homeownership levels are at historic highs;
- Manufacturing activity is increasing;
- Inflation and interest rates are low;
- Over 360,000 jobs have been created in the past five months;
- Unemployment claims – both initial claims and continuing claims – are well off their peaks of last year, indicating improvement in the labor market;

• In the middle of this month, the Dow closed at a 32-month-high. This translates into more than three trillion dollars of growth in value in the markets.

These economic indicators all point to the same conclusion: economic growth is robust and will be sustained.

However, there is more to do. We are not, by any means, satisfied.

There are still Americans who want to find work and cannot... and this Administration will not rest until that most critical need is met and until every American looking for work can find a job.

The President's proposed budget, which we sent up to the hill a few weeks ago, addresses that need by continuing to focus on improving our economy... by making those tax cuts permanent, encouraging small business growth and investment. And by holding the line on spending. This combined effort is designed to cut our deficit in half in five years.

This issue of continuing to grow the economy is so essential... and I know that you understand that.

I see credit unions as playing an important role in economic growth.

Your dedication to small-business lending is one of the major reasons why I say that.

Small business is at the foundation of this great economy, and credit unions have been there for entrepreneurs when they needed you the most.

As of last year, credit unions were welcomed into the SBA lending programs, and I hope that has helped out both you and America's entrepreneurs as much as this Administration hoped it would.

You know as well as I do: small business is where the jobs come from. We estimate that between two-thirds and three-quarters of recent net new jobs are coming from that sector.

That's why we want to make small business tax cuts permanent, and that's why I want to commend the credit union community for financing America's hard-working small-business owners!

There is something that is especially true when we talk about your lending activity to the entrepreneurial community... and that is the fact that, as a group, you really understand the value of relationships, and of working together... it makes you unique.

This quality makes you valuable to your customers, and over the last couple of years has made you valuable to your country... because you're working so well with the Treasury Department... we're partners, working together to fight the war on terror.

Out of the horror of September 11th, 2001, came a tremendous resolve in the financial community to cut off the terrorists' lifeblood: their money.

Institutions large and small have committed themselves to the task.

America's credit unions have done everything that the Treasury Department has asked of you during this fight, and I want to personally thank you for your efforts. In a very real sense, together we have forged a partnership in this fight.

For example, your compliance with the information sharing provisions of Section 314 of the Patriot Act has been exemplary.

Under our 314 process, law enforcement provides the names of suspected terrorists or significant money launderers to Treasury's Financial Crimes Enforcement Network (FinCEN), which scrubs the names and, if appropriate, sends them on to you. We've asked that you then search your recent account and transaction records for potential matches, and report them back to FinCEN.

You've done it, and our country is safer because of it.

We understand that the 314 process is an extraordinary tool... it is one that provides law enforcement with valuable leads to follow the money trail. And without your help it would be useless.

We've also asked you to establish risk-based procedures to verify the identity of your customers who open accounts, pursuant to section 326 of the Patriot Act. While we insist that you form a reasonable belief as to the customer's identity, we have also worked hard to ensure that the regulation give you the flexibility to decide which forms of identification you will accept to verify customer identity. This reflects our judgment that you are in the best position to make such decisions. We believe this flexibility enhances the effectiveness of this regulation.

And we're always looking for ways to provide you with more and better guidance concerning FinCEN's regulations. This is our part of the bargain, our half of the partnership. So let's keep up the dialog... let us know when we're not clear, or when we can do better – because the better our regulations are understood by you, the more successful our critical enforcement efforts will be.

So please know that we appreciate our working relationship on the war on terror, and that we view you as a partner in other critical ways, as well.

You're a partner in economic growth, as I mentioned before.

You're also a partner in the effort to increase financial literacy in this country.

You are closer to your customers than a lot of financial institutions are. You therefore have an opportunity to contribute in a unique way to financial literacy efforts.

I'm pleased to say that a multitude of individuals and organizations like yours– across the many agencies of government, among members of Congress, and throughout the private sector – are dedicating major resources to improve financial literacy in America.

In other words, there is a serious movement afoot, and it is a good one.

President Bush is dedicated to this cause, which is why the Treasury Department created the Office of Financial Education in May of 2002.

Its work was then recognized by Congress in Title Five of the Fair and Accurate Credit Transactions Act, which the President signed this past December.

Treasury's Financial Education Office now serves as the supporting office for a new Financial Literacy Commission, whose work is to complement, encourage and sometimes coordinate the work of the many individuals and institutions that are committed to greater financial literacy in America.

I would also like to see the Commission identify some areas that need the most help, the quickest... and credit unions can help us do that.

For example: I think we have a tremendous opportunity to start fresh with a new generation… to ensure that tomorrow's young adults understand how important it is to save, and how to protect themselves from identity theft, in the same way that they understand the basics of physical health or road safety.

There is a tremendous interest on the part of high school students to learn the financial facts of life: how to manage a credit card, how to save and invest, how important it is to save for retirement at the beginning of a career, not at the end.

When you consider the fact that the financial tragedy of bankruptcy is growing fastest among young adults in their early 20s, it becomes clear that we must work to satisfy the natural desire of young people to learn now and therefore reduce this problem for the next generation.

Another group that has an immediate need is our population of new immigrants to this country.

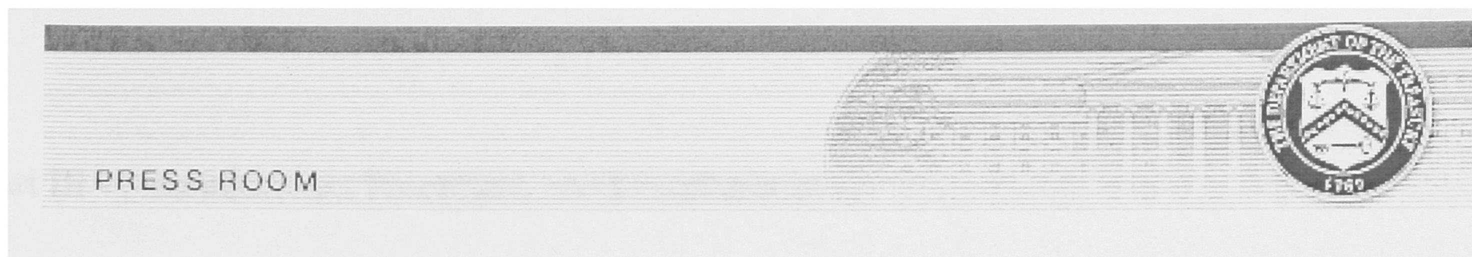
Many new immigrants come to America from places where consumer financial services are not common, where checking accounts and credit cards and mortgage loans are virtually unknown, and where a bank is not seen as a safe place to put your money. They do not know how to get involved in the financial mainstream here, and so they remain outside of the mainstream, prey to the loan sharks and the financial predators.

You and your staff are uniquely positioned to reach out to these groups and others in need of financial education to help bring them into the financial mainstream, where they can safely build up their assets, invest and save for their futures and their children's futures.
As with so many other things, we accomplish the most when we work together. Whether it's fighting terrorists, or teaching teenagers about financial responsibility, or helping entrepreneurs pursue their American Dreams.

I'm glad to work with the nation's credit unions on all these efforts.

I thank you for the work you do, and the chance to speak to you today.

Have a great conference.



FROM THE OFFICE OF PUBLIC AFFAIRS

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February 24, 2004
JS-1189

Treasury and IRS Issue Proposed Rules on Student Exception to FICA Employment Tax

Today, Treasury and the IRS issued proposed regulations concerning the exception from FICA employment tax for students employed by the school, college or university where the student is pursuing a course of study. The proposed regulations expand upon existing regulations and guidance, including clarifying that whether an organization is a school, college or university is determined based on the primary function of the organization. The proposed regulations also clarify that determination of whether employees are students for purposes of the exclusion is made by examining the individual's employment relationship with the employer to determine if employment or education is predominant in the relationship.

The regulations make conforming changes for purposes of Federal unemployment taxes, for which there is an identical exception. These rules have particular relevance in determining whether a medical resident providing services to a hospital is considered a student for employment tax purposes.

In addition, the IRS released a notice suspending Revenue Procedure 98-16, which provided that students enrolled at least half-time at certain institutions of higher education qualify for the student FICA exception. The notice proposes a new revenue procedure that is consistent with the proposed regulations and provides interim reliance. Colleges and universities that have been relying on the safe harbor provided in Rev. Proc. 98-16 will generally be unaffected by this guidance.

Related Documents:

- The text of Notice 2004-12

Part III - Administrative, Procedural, and Miscellaneous

Proposed Revenue Procedure Regarding Services that Qualify For the Student FICA Exception

Notice 2004-12

I. Overview and Purpose

This notice contains a proposed revenue procedure providing a safe harbor that certain institutions of higher education, and certain affiliated organizations can use in applying the exception for services performed by a student provided under § 3121(b)(10) of the Internal Revenue Code (student FICA exception). A previous version of this safe harbor was issued in Rev. Proc. 98-16, 1998-1 C.B. 403. However, the Service has recently proposed amendments to the Employment Tax Regulations interpreting § 3121(b)(10) in order to clarify specific issues that have arisen with taxpayers and in litigation (see proposed regulations § 31.3121(b)(10)-2(c), (d), and (e) published in the Federal Register on February 25, 2004 (XX Fed. Reg. XXXX)). In order to provide guidance that is consistent with the proposed regulations in all respects, the Service is suspending Rev. Proc. 98-16 and proposing to replace it with the revenue procedure contained in this notice.

The proposed revenue procedure updates the safe harbor of Rev. Proc. 98-16 in several respects that align it with the proposed regulations. First, the proposed revenue procedure adds a primary function requirement to the definition of an institution of higher education. Section 3121(b)(10) applies only to services performed in the employ of a school, college or university, or an affiliated § 509(a)(3) organization. Under the proposed regulations and the new safe harbor, an organization can be a school, college or university only if its primary function is to conduct educational activities. Thus, in order to take advantage of the safe harbor in the revenue procedure, an institution must satisfy not only the Department of Education's regulations at 34 C.F.R. § 600.4 and satisfy the accreditation requirements of 34 C.F.R. § 600.2, as was required in Rev. Proc. 98-16, but also must have education and instruction as its primary function. The primary function requirement may make the exception under § 3121(b)(10) unavailable to certain institutions of higher education that are embedded within a larger organization like a hospital or museum.

Second, the proposed revenue procedure does not permit an institution to apply the student

FICA exception to services performed by an employee who regularly works 40 or more hours per week. Under the existing regulations, services fall within the student FICA exception only if they are performed incident to and for the purpose of pursuing a course of study. The proposed regulations clarify that an individual who regularly works forty or more hours per week has the status of a career employee, and, accordingly, is not performing services incident to and for the purpose of pursuing a course of study. The proposed revenue procedure follows the proposed regulations. The student FICA exception generally, and the safe harbor provided by the proposed revenue procedure specifically, are still available for services performed by an employee who on occasion works 40 or more hours per week and otherwise meets the requirements of the safe harbor.

Third, the proposed revenue procedure provides that an individual has career employee status if the individual is a "professional employee." The proposed regulations provide that a professional employee for purposes of the student FICA exception is an employee whose primary duty consists of the performance of services requiring knowledge of an advanced type in a field of science or learning, whose work requires the consistent exercise of discretion and judgment in its performance, and whose work is predominantly intellectual and varied in character. The proposed revenue procedure follows the proposed regulations.

Fourth, the proposed revenue procedure expands the terms of employment that result in status as a career employee. Rev. Proc. 98-16 provided that an individual was to be considered a career employee if the employee was eligible to participate in one of several types of retirement plans, eligible for reduced tuition (with certain exceptions), or otherwise classified by the institution of higher education as a career employee. The proposed regulations adopt the same criteria for identifying individuals who have the status of a career employee and adds to the list eligibility for a number of other benefits. The proposed revenue procedure follows the proposed regulations, adding the additional criteria that cause an individual to have career employee status and fall outside the scope of the safe harbor. Employees considered as having the status of a career employee per se cannot have the status of a student for purposes of the student FICA exception.

Fifth, and finally, the proposed revenue procedure provides that an employee has career employee status if the individual is required to be licensed under state or local law in order to perform the services the individual provides to the school, college or university. The proposed revenue procedure follows the proposed regulation.

II. Request for Comments

Comments are requested on the proposed revenue procedure. Comments may be submitted on or before May 25, 2004, to Internal Revenue Service, PO Box 7604, Washington, DC 20044, Attn: CC:PA:LPD:PR (Notice 2004-12), Room 5203. Submissions may also be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to the Courier=s Desk at 1111 Constitution Avenue, NW., Washington, DC 20224, Attn: CC:PA:LPD:PR (Notice 2004-12), Room 5203. Submissions may also be sent electronically via the internet to the following email address: Notice.comments@irscounsel.treas.gov. Include the notice number (Notice 2004-12) in the subject line.

III. Effect on Other Documents

Rev. Proc. 98-16 is suspended effective February 25, 2004.

IV. Effective Date

The Service intends to issue a final revenue procedure at the same time that the proposed regulations under § 3121(b)(10) are finalized. Until a final version of the proposed revenue procedure is issued, taxpayers may rely on the proposed revenue procedure with respect to services performed on or after February 25, 2004 (the date prop. Reg. § 31.3121(b)(10)-2(c) - (f) (XX FR XXXX) was published in the Federal Register).

V. Proposed Revenue Procedure

SECTION 1. PURPOSE

This revenue procedure sets forth generally applicable standards for determining whether service in the employ of certain public or private nonprofit schools, colleges, universities, or affiliated organizations described in § 509(a)(3) of the Internal Revenue Code (the Code) performed by a student qualifies for the exception from Federal Insurance Contributions Act (FICA) tax provided under § 3121(b)(10) of the Code (Student FICA exception). These standards are intended to provide objective and administrable guidelines for determining employment tax liability.

SECTION 2. SCOPE

.01 Institutions of higher education typically distinguish between career employees and student employees. Sections 5 and 6 of this revenue procedure contain generally applicable standards for determining whether or not services performed by employees of certain institutions of higher education are eligible for the Student FICA exception.

.02 The standards contained in this revenue procedure do not apply to employees who are postdoctoral

students, postdoctoral fellows, medical residents, or medical interns because the services performed by these employees cannot be assumed to be incident to and for the purpose of pursuing a course of study. The employment activities of these individuals overlaps with the activities comprising the course of study, and thus it is not appropriate to apply the standards of this revenue procedure to these individuals.

.03 The standards contained in this revenue procedure may not constitute the exclusive method for determining whether the Student FICA exception applies. If the standard for qualifying for the exclusion described in section 6 of this revenue procedure (providing generally that an employee enrolled at least half-time at an institution of higher education has the status of student) is not met, whether or not service in the employ of a school, college, university, or affiliated organization described in § 509(a)(3) of the Code will qualify for the Student FICA exception will depend on consideration of all the facts and circumstances.

SECTION 3. BACKGROUND

.01 Sections 3101 and 3111 of the Code impose social security and Medicare taxes (FICA taxes) on employees and employers, respectively, equal to a percentage of the wages received by an individual with respect to employment.

.02 Section 3121(a) of the Code defines "wages" for purposes of FICA taxes as all remuneration for employment, with certain exceptions. Section 3121(b) of the Code defines "employment" as services performed by an employee for an employer, with certain exceptions.

.03 Section 3121(b)(10) of the Code excepts from the definition of employment services performed in the employ of a school, college, or university (whether or not that organization is exempt from income tax), or an affiliated organization described in § 509(a)(3) of the Code, if the services are performed by a student who is enrolled and regularly attending classes at that school, college or university. Remuneration for services excluded from the definition of employment under § 3121(b)(10) of the Code is not subject to FICA taxes.

.04 Section 31.3121(b)(10)-2 of the Employment Tax Regulations provides that whether an employee has the status of a student is determined on the basis of the employee's relationship with the school, college, or university for which the services are being performed. An employee who performs services in the employ of a school, college, or university as an incident to and for the purpose of pursuing a course of study at the school, college, or university has the status of a student in the performance of those services. Services that are not incident to and for the purpose of pursuing a course of study do not qualify for the exception. If the employee performs services as an incident to and for the purpose of pursuing a course of study and, therefore, has the status of a student, the amount of

remuneration for services performed by the employee, the type of services performed by the employee, and the place where the services are performed are immaterial for purposes of the Student FICA exception.

.05 Section 218 of the Social Security Act (the Act), 42 U.S.C. section 418, allows states to provide Social Security coverage for services performed by students for the public school the student is attending under agreements established with the Social Security Administration. If a state has exercised its option under § 218 of the Act to provide for coverage of student services, § 3121(b)(10) of the Code provides that those services will not qualify for the Student FICA exception.

SECTION 4. CERTAIN INSTITUTIONS OF HIGHER EDUCATION

.01 The standards contained in this revenue procedure apply to "institutions of higher education" meeting the requirements of § 31.3121(b)(10)-2(c) of the proposed Employment Tax Regulations. For purposes of this revenue procedure, the term "institution of higher education" includes any public or private nonprofit school, college, university within the meaning of prop. Reg. § 31.3121(b)(10)-2(c), or affiliated organization described in § 509(a)(3) of the Code, that meets the requirements set forth in Department of Education regulations at 34 C.F.R. § 600.4, as amended from time to time, and that is accredited or preaccredited by a nationally recognized accrediting agency as defined in the Department of Education regulations at 34 C.F.R. § 600.2.

.02 Services for other institutions may also be eligible for the Student FICA exception. Thus, for example, services performed by a student for a secondary school may be eligible for the Student FICA exception. Whether or not services for other institutions, such as secondary schools, qualify for the Student FICA exception is determined based on the facts and circumstances of each case.

SECTION 5. STUDENT FICA EXCEPTION NOT AVAILABLE FOR EMPLOYEES WITH CAREER EMPLOYEE STATUS

.01 Services performed by individuals with career employee status are not eligible for the Student FICA exception under the standard in section 6 of this revenue procedure because their services are not incident to and for the purpose of pursuing a course of study. See prop. Reg. § 31.3121(b)(10)-2(d)(3)(ii).

.02 Career employee status. Services of an employee with career employee status are not incident to and for the purpose of pursuing a course of study. An employee may be considered to have career employee status based on the employee's hours worked, whether the employee is a "professional employee," the employee's terms of employment, or whether the employee is licensed under state or local law to work in the field in which the employee performs services. These standards are set forth in

prop. Reg. § 31.3121(b)(10)-2(d)(3)(ii). An employee has career employee status if the employee is described in paragraph (1), (2), (3), or (4) of this section.

(1) Hours worked. An employee has the status of a career employee if the employee regularly performs services 40 hours or more per week.

(2) Professional employee. An employee has the status of a career employee if the employee is a professional employee. A professional employee is an employee--

(a) Whose primary duty consists of the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study, as distinguished from a general academic education, from an apprenticeship, and from training in the performance of routine mental, manual, or physical processes.

(b) Whose work requires the consistent exercise of discretion and judgment in its performance; and

(c) Whose work is predominantly intellectual and varied in character (as opposed to routine mental, manual, mechanical, or physical work) and is of such character that the output produced or the result accomplished cannot be standardized in relation to a given period of time.

(3) Terms of employment. An employee's terms of employment may indicate that the employee has career employee status. An employee with career employee status includes any employee who is--

(a) Eligible to receive vacation, sick leave, or paid holiday benefits;

(b) Eligible to participate in any retirement plan described in § 401(a) of the Code that is established or maintained by the employer; or would be eligible to participate if age and service requirements were met;

(c) Eligible to participate in an arrangement described in § 403(b) of the Code, or would be eligible to participate if age and service requirements were met;

(d) Eligible to participate in a plan described under § 457(a), or would be eligible to participate if age and service requirements were met;

(e) Eligible for reduced tuition (other than qualified tuition reduction under § 117(d)(5) of the Code provided to a teaching or research assistant who is a graduate student) because of the individual's employment relationship with the institution;

(f) Eligible to receive employee benefits described under § 79 (life insurance), 127 (qualified

educational assistance), 129 (dependent care assistance programs), or 137 (adoption assistance); or

(g) Classified by the employer as a career employee.

(4) Licensure. An employee is a career employee if the employee is required to be licensed under state or local law to work in the field in which the employee performs services.

.03 If an individual performs services in multiple job positions, the individual will be deemed to have career employee status with respect to all of the positions if the individual has career employee status in any one or more of the job positions.

SECTION 6. STANDARDS APPLICABLE TO UNDERGRADUATE AND GRADUATE STUDENTS

.01 An individual who is a half-time undergraduate student or a half-time graduate or professional student and who does not have the status of a career employee will qualify for the Student FICA exception under this revenue procedure with respect to services performed at or for an institution of higher education described in section 4 of this revenue procedure in which they are enrolled or at affiliated organizations described in § 509(a)(3) of the Code. Services performed by a student for any other employer are not covered by the standards of this revenue procedure.

.02 An individual is deemed to be a half-time undergraduate or half-time graduate or professional student if the individual does not have the status of a career employee status and is an undergraduate or graduate student who is in the last semester, trimester, or quarter of a course of study requiring at least two semesters, trimesters, or quarters to complete and is enrolled in the number of credit or unit hours needed to complete the requirements for obtaining a degree, certificate, or other recognized educational credential offered by that institution of higher education even if enrolled in less than half the number required of full-time students.

.03 The determination of student status should be made at the end of the drop-add period and may be adjusted thereafter at the institution of higher education's option. The determination of student status for payroll periods ending before the end of the drop-add period may be based on the number of semester, trimester, or quarter hours being taken at the end of the registration period for that semester, trimester, or quarter.

.04 If an individual is described in section 6.01 or 6.02 of this revenue procedure, services performed by the individual are eligible for the Student FICA exception with respect to all services performed during all payroll periods of a month or less that fall wholly or partially within the academic term.

.05 The Student FICA exception does not apply to services performed by an individual who is not enrolled in classes during school breaks of more than five weeks (including summer breaks of more than five weeks), other than services described in section 6.04. See Rev. Rul. 72-142, 1972-1 C.B. 317, and Rev. Rul. 74-109, 1974-1 C.B. 288. However, the Student FICA exception applies to employment which continues during normal school breaks of 5 weeks or less during which the individual is not eligible for the Student FICA exception pursuant to section 6.01 of this revenue procedure provided that the individual qualifies for the Student FICA exception pursuant to section 6.01 of this revenue procedure on the last day of classes or examinations preceding the break and is eligible to enroll in classes for the first academic period following the break.

.06 If the standards of this revenue procedure are met (and section 8 does not apply), the amount of remuneration for services performed by the employee, the type of services performed by the employee, and the place where the services are performed are immaterial. If the services performed by a student otherwise described in section 6.01 or 6.02 are covered under an agreement pursuant to section 218 of the Act, the Student FICA exception does not apply.

.07 For provisions relating to domestic service performed by a student in a local college club, or local chapter of a college fraternity or sorority, see § 31.3121(b)(2)-1.

SECTION 7. DEFINITIONS

For purposes of the standard contained in section 6 of this revenue procedure, the following definitions must be used. For purposes of the following definitions, the term "institution of higher education" means an institution of higher education as defined in section 4 of this revenue procedure.

.01 Undergraduate student. The term "undergraduate student" has the meaning attributed to that term in the Department of Education regulations at 34 C.F.R. section 674.2.

.02 Half-time undergraduate student. The term "half-time undergraduate student" has the meaning attributed to that term in the Department of Education regulations at 34 C.F.R. section 674.2.

.03 Graduate or professional student. The term "graduate or professional student" means a student who--

(1) is enrolled at an institution of higher education for the purpose of obtaining a degree, certificate, or other recognized educational credential above the baccalaureate level or is enrolled in a program leading to a professional degree;

(2) has completed the equivalent of at least three years of full-time study at an institution of higher

education, either prior to entrance into the program or as part of the program itself; and

(3) is not a postdoctoral student, postdoctoral fellow, medical resident, or medical intern.

.04 Half-time graduate or professional student. The term "half-time graduate or professional student" means an enrolled graduate or professional student, as defined in section 7.03 of this revenue procedure, who is carrying at least a half-time academic workload at an institution of higher education as determined by that institution according to its own standards and practices.

SECTION 8. ANTI-ABUSE RULE

The standards in this revenue procedure must be applied in a reasonable manner, consistent with the purpose of excluding from employment only services that are performed as an incident to and for the purpose of pursuing a course of study at an institution of higher education as defined in section 4 of this revenue procedure. If the standards are inappropriately applied in a manner that conflicts with this underlying purpose so as to manipulate or mischaracterize the nature of the relationship between an employee and an institution of higher education, resulting in the improper avoidance of payment of FICA taxes, then whether the Student FICA exception applies will be determined on the basis of all the facts and circumstances, rather than on the basis of the specific standards set forth in section 6 of this revenue procedure. For example, the standards would be inappropriately applied through the manipulation of the relationship between employees and the institution of higher education if a university claimed that the Student FICA exception applied to research laboratory workers, who had been career employees, but were converted to non-career status and required to enroll in a certificate program granting six credit hours per semester for work experience in the laboratory. As another example, if an individual who was not a student worked for a university on a full-time basis for many years, in a job generally performed by non-students (but nonetheless failed to meet the literal definition of career employee), and then enrolled at the university for six credit hours of course work per semester while continuing the full-time work in the same job, it may not be appropriate to apply the standards of this revenue procedure to conclude that the individual's work has become incident to and for the purpose of pursuing a course of study solely because the individual enrolled for this course work. In both of these examples, whether the work is performed incident to and for the purpose of pursuing a course of study must be determined on the basis of all the relevant facts and circumstances.

SECTION 9. EFFECTIVE DATE

This revenue procedure is effective for services performed on or after February 25, 2004 (the date prop. Reg. § 31.3121(b)(10)-2(c) - (f) (XX FR XXXX) was published in the Federal Register).

The principal author of this notice is Stephen D. Suetterlein of the Office of Associate Chief

Counsel (Tax Exempt & Government Entities). However, other personnel from the Service and Treasury Department participated in the development of this notice. For further information regarding this notice contact Mr. Suetterlein at (202) 622-6040 (not a toll-free call).

FROM THE OFFICE OF PUBLIC AFFAIRS

February 24, 2004
JS-1190

United States Designates bin Laden Loyalist

The Treasury Department today announced that Shaykh Abd-al-Majid AL-ZINDANI, a loyalist to Usama bin Laden and supporter of al-Qaeda, has been designated by the United States as a Specially Designated Global Terrorist under the authority of Executive Order 13224 and the International Emergency Economic Powers Act. His name will be submitted to the UN Security Council's 1267 Committee's consolidated list because of his support to bin Laden and al-Qaeda.

"With this action, the international community's drumbeat against terrorist financiers continues to grow louder and the financial noose around al-Qaeda continues to grow tighter," said Juan Zarate, Deputy Assistant Secretary for Terrorist Financing and Financial Crime.

The U.S. has credible evidence that AL-ZINDANI, a Yemeni national, supports designated terrorists and terrorist organizations.

AL-ZINDANI has a long history of working with bin Laden, notably serving as one of his spiritual leaders. In this leadership capacity, he has been able to influence and support many terrorist causes, including actively recruiting for al-Qaeda training camps. Most recently, he played a key role in the purchase of weapons on behalf of al-Qaeda and other terrorists.

AL-ZINDANI also served as a contact for Ansar al-Islam (AI), a Kurdish-based terrorist organization linked to al-Qaeda, which is included in the UN 1267 sanctions Committee list.

AL-ZINDANI is the founder and leader of the Al Iman University in Sanaa, Yemen, which has over 5,000 enrollees. Al Iman students are suspected of being responsible, and were arrested, for recent terrorist attacks, including the assassination of three American missionaries and the assassination of the number two leader for the Yemeni Socialist party, Jarallah Omar. Notably, John Walker Lindh was also a student at Al Iman University before he joined the Taliban.

AL-ZINDANI, born circa 1950, has used the aliases Abdelmajid Al-Zindani and Shaykh Abd Al-Majid Al-Zindani. He holds a Yemen passport, no. A005487, which was issued on August 13, 1995.

Executive Order 13224 provides means to disrupt the support network that funds terrorism. Under this order, the United States government may block the assets of individuals and entities providing support, financial or otherwise, to designated terrorists and terrorist organizations. Blocking actions are critical to combating the financing of terrorism.

When a blocking action is put into place, any assets that exist in the formal financial system at the time of the orders are frozen. Blocking actions serve additional functions as well, e.g., they act as a deterrence for non-designated parties who might otherwise be willing to finance terrorist activity; expose terrorist financing "money trails" that may generate leads to previously unknown terrorist cells and financiers; disrupt terrorist financing networks by encouraging designated terrorist supporters to disassociate themselves from terrorist activity and renounce their affiliation with terrorist groups; terminate terrorist cash flows by shutting down the

pipelines used to move terrorist- related assets; force terrorist to use alternative, more costly, and higher-risk means of financing their activities; and engender international cooperation and compliance with obligations under UN Security Council Resolutions.

Designation under the UN Security Council's 1267 Committee's consolidated list will trigger international obligations on all member countries, requiring them to take steps to prevent designated individuals and entities from continuing to fund or otherwise support terrorism. It is also a critical action to publicly identify these supporters of terrorism, providing warning to other entities that they are prohibited from doing business with them.

The Treasury Department is committed to stopping terrorism by taking action against those who fund it. With this designation, 351 individuals and entities will have been designated under President Bush's Executive Order aimed at freezing the assets of terrorists and their supporters – Executive Order 13224. At least $139 million in assets has been kept out of the control of terrorists as a result of efforts by the United States and its allies.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 25, 2004
JS-1191

Testimony of
Barbara M. Angus, International Tax Counsel,
United States Department of the Treasury
before the Senate Committee on Foreign Relations
on Pending Income Tax Agreements
FEBRUARY 25, 2004

Mr. Chairman and distinguished Members of the Committee, I appreciate the opportunity to appear today at this hearing to recommend, on behalf of the Administration, favorable action on two income tax treaties that are pending before this Committee. We appreciate the Committee's interest in these agreements as demonstrated by the scheduling of this hearing.

This Administration is dedicated to eliminating unnecessary barriers to cross-border trade and investment. The primary means for eliminating tax barriers to trade and investment are bilateral tax treaties. Tax treaties eliminate barriers by providing greater certainty to taxpayers regarding their potential liability to tax in the foreign jurisdiction; by allocating taxing rights between the two jurisdictions so that the taxpayer is not subject to double taxation; by reducing the risk of excessive taxation that may arise because of high gross-basis withholding taxes; and by ensuring that taxpayers will not be subject to discriminatory taxation in the foreign jurisdiction. The international network of over 2000 bilateral tax treaties has established a stable framework that allows international trade and investment to flourish. The success of this framework is evidenced by the fact that countless cross-border transactions, from investments in a few shares of a foreign company by an individual to multi-billion dollar purchases of operating companies in a foreign country, take place each year, with only a relatively few disputes regarding the allocation of tax revenues between governments.

The Administration believes that these agreements with Japan and Sri Lanka would provide significant benefits to the United States and to our treaty partners, as well as our respective business communities. The tax treaty with Japan is a critically important modernization of the economic relationship between the world's two largest economies. The agreement with Sri Lanka represents the first tax treaty between our two countries, and reflects our continuing commitment to extending our treaty network to emerging economies. We urge the Committee and the Senate to take prompt and favorable action on both agreements.

Purposes and Benefits of Tax Treaties

Tax treaties provide benefits to both taxpayers and governments by setting out clear ground rules that will govern tax matters relating to trade and investment between the two countries. A tax treaty is intended to mesh the tax systems of the two countries in such a way that there is little potential for dispute regarding the amount of tax that should be paid to each country. The goal is to ensure that taxpayers do not end up caught in the middle between two governments, each of which claims taxing jurisdiction over the same income. A treaty with clear rules addressing the most likely areas of disagreement minimizes the time the two governments (and taxpayers) spend in resolving individual disputes.

One of the primary functions of tax treaties is to provide certainty to taxpayers regarding the threshold question with respect to international taxation: whether the taxpayer's cross-border activities will subject it to taxation by two or more countries. Treaties answer this question by establishing the minimum level of economic activity that must be engaged in within a country by a resident of the other country before the first country may tax any resulting business profits. In general terms, tax treaties provide that if the branch operations in a foreign country have sufficient substance and continuity, the country where those activities occur will have primary (but not exclusive) jurisdiction to tax. In other cases, where the operations in the foreign country are relatively minor, the home country retains the sole jurisdiction to tax its residents. In the absence of a tax treaty, a U.S. company operating a branch or division or providing services in another country might be subject to income tax in both the United States and the other country on the income generated by such operations. Although the United States generally provides a credit against U.S. tax liability for foreign taxes paid, there remains potential for resulting double taxation that could make an otherwise attractive investment opportunity unprofitable, depriving both countries of the benefits of increased cross-border investment.

Tax treaties protect taxpayers from potential double taxation through the allocation of taxing rights between the two countries. This allocation takes several forms. First, the treaty has a mechanism for resolving the issue of residence in the case of a taxpayer that otherwise would be considered to be a resident of both countries. Second, with respect to each category of income, the treaty assigns the "primary" right to tax to one country, usually (but not always) the country in which the income arises (the "source" country), and the "residual" right to tax to the other country, usually (but not always) the country of residence of the taxpayer. Third, the treaty provides rules for determining which country will be treated as the source country for each category of income. Finally, the treaty provides rules limiting the amount of tax that the source country can impose on each category of income and establishes the obligation of the residence country to eliminate double taxation that otherwise would arise from the exercise of concurrent taxing jurisdiction by the two countries.

As a complement to these substantive rules regarding allocation of taxing rights, tax treaties provide a mechanism for dealing with disputes or questions of application that arise after the treaty enters into force. In such cases, designated tax authorities of the two governments – known as the "competent authorities" in tax treaty parlance – are to consult and reach an agreement under which the taxpayer's income is allocated between the two taxing jurisdictions on a consistent basis, thereby preventing the double taxation that might otherwise result.

The U.S. competent authority under our tax treaties is the Secretary of the Treasury. That function has been delegated to the Director, International (LMSB) of the Internal Revenue Service.

In addition to reducing potential double taxation, treaties also reduce "excessive" taxation by reducing withholding taxes that are imposed at source. Under U.S. domestic law, payments to non-U.S. persons of dividends and royalties as well as certain payments of interest are subject to withholding tax equal to 30 percent of the gross amount paid. Most of our trading partners impose similar levels of withholding tax on these types of income. This tax is imposed on a gross, rather than net, amount. Because the withholding tax does not take into account expenses incurred in generating the income, the taxpayer frequently will be subject to an effective rate of tax that is significantly higher than the tax rate that would be applicable to net income in either the source or residence country. The taxpayer may be viewed, therefore, as having suffered "excessive" taxation. Tax treaties alleviate this burden by setting maximum levels for the withholding tax that the treaty partners may impose on these types of income or by providing for exclusive residence-country taxation of such income through the elimination of source-country withholding tax. Because of the excessive taxation that withholding taxes can represent, the United States seeks to include in tax treaties provisions that substantially reduce or eliminate source-country withholding taxes.

Our tax treaties also include provisions intended to ensure that cross-border investors do not suffer discrimination in the application of the tax laws of the other

country. This is similar to a basic investor protection provided in other types of agreements, but the non-discrimination provisions of tax treaties are specifically tailored to tax matters and therefore are the most effective means of addressing potential discrimination in the tax context. The relevant tax treaty provisions provide guidance about what "national treatment" means in the tax context by explicitly prohibiting types of discriminatory measures that once were common in some tax systems. At the same time, tax treaties clarify the manner in which possible discrimination is to be tested in the tax context. Particular rules are needed here, for example, to reflect the fact that foreign persons that are subject to tax in the host country only on certain income may not be in the same position as domestic taxpayers that may be subject to tax in such country on all their income.

Tax treaties also include provisions dealing with more specialized situations, such as rules coordinating the pension rules of the tax systems of the two countries or addressing the treatment of employee stock options, Social Security benefits, and alimony and child support in the cross-border context. These provisions are becoming increasingly important as the number of individuals who move between countries or otherwise are engaged in cross-border activities increases. While these subjects may not involve substantial tax revenue from the perspective of the two governments, rules providing clear and appropriate treatment can be very important to each of the individual taxpayers who are affected.

In addition, tax treaties include provisions related to tax administration. A key element of U.S. tax treaties is the provision addressing the exchange of information between the tax authorities. Under tax treaties, the competent authority of one country may request from the other competent authority such information as may be necessary for the proper administration of the country's tax laws; the requested information will be provided subject to strict protections on the confidentiality of taxpayer information. Because access to information from other countries is critically important to the full and fair enforcement of the U.S. tax laws, information exchange is a priority for the United States in its tax treaty program. If a country has bank secrecy rules that would operate to prevent or seriously inhibit the appropriate exchange of information under a tax treaty, we will not conclude a treaty with that country. In fact, information exchange is a matter we raise with the other country before commencement of formal negotiations because it is one of a very few matters that we consider non-negotiable.

Tax Treaty Negotiating Priorities and Process

The United States has a network of 56 bilateral income tax treaties covering 64 countries. This network includes all 29 of our fellow members of the OECD and covers the vast majority of foreign trade and investment of U.S. businesses. It is, however, appreciably smaller than the tax treaty networks of some other countries. There are a number of reasons for this.

The primary constraint on the size of our tax treaty network may be the complexity of the negotiations themselves. The various functions performed by tax treaties, and particularly the goal of meshing two different tax systems, make the negotiation process exacting and time-consuming.

A country's tax policy, as reflected in its domestic tax legislation as well as its tax treaty positions, reflects the sovereign choices made by that country. Numerous features of the treaty partner's particular tax legislation and its interaction with U.S. domestic tax rules must be considered in negotiating an appropriate treaty. Examples include whether the country eliminates double taxation through an exemption system or a credit system, the country's treatment of partnerships and other transparent entities, and how the country taxes contributions to pension funds, the funds themselves, and distributions from the funds. A treaty negotiation must take into account all of these and many other aspects of the treaty partner's tax system in order to arrive at an agreement that accomplishes the United States' tax treaty objectives.

In any tax treaty negotiation, the two countries may come to the table with very different views of what a final treaty should provide. Each country will have its own list of positions that it considers non-negotiable. The United States, which insists

on effective anti treaty-shopping and exchange of information provisions, and which must accommodate the uniquely complex U.S. tax laws, probably has more non-negotiable positions than most countries. For example, the United States insists on inclusion of a special provision – the "saving clause" – which permits the United States to tax its citizens and residents as if the treaty had not come into effect, as well as special provisions that allow the United States to apply domestic tax rules covering former citizens and long-term residents.

Other U.S. tax law provisions that can complicate negotiations include the branch profits tax and the branch level interest tax, rules regarding our specialized investment vehicles, such as real estate mortgage investment conduits, real estate investment trusts and regulated investment companies, and the Foreign Investors in Real Property Tax Act rules. As our international tax rules become more and more complicated, the number of special tax treaty rules that are required increases as well.

Obtaining the agreement of our treaty partners on provisions of importance to the United States sometimes requires other concessions on our part. Similarly, other countries sometimes must make concessions to obtain our agreement on matters that are critical to them. In most cases, the process of give-and-take produces a document that is the best tax treaty that is possible with that other country. In other cases, we may reach a point where it is clear that it will not be possible to reach an acceptable agreement. In those cases, we simply stop negotiating with the understanding that negotiations might restart if circumstances change. Each treaty that we present to the Senate represents not only the best deal that we believe we can achieve with the particular country, but also constitutes an agreement that we believe is in the best interests of the United States.

In establishing our negotiating priorities, our primary objective is the conclusion of tax treaties or protocols that will provide the greatest economic benefit to the United States and to U.S. taxpayers. We communicate regularly with the U.S. business community, seeking input regarding the areas in which treaty network expansion and improvement efforts should be focused and information regarding practical problems encountered by U.S. businesses with respect to the application of particular treaties and the application of the tax regimes of particular countries.

The U.S. commitment to including comprehensive provisions designed to prevent "treaty shopping" in all of our tax treaties is one of the keys to improving our overall treaty network. Our tax treaties are intended to provide benefits to residents of the United States and residents of the particular treaty partner on a reciprocal basis. The reductions in source-country taxes agreed to in a particular treaty mean that U.S. persons pay less tax to that country on income from their investments there and residents of that country pay less U.S. tax on income from their investments in the United States. Those reductions and benefits are not intended to flow to residents of a third country. If third-country residents can exploit one of our treaties to secure reductions in U.S. tax, the benefits would flow only in one direction. Such use of treaties is not consistent with the balance of the deal negotiated. Moreover, preventing this exploitation of our treaties is critical to ensuring that the third country will sit down at the table with us to negotiate on a reciprocal basis, so that we can secure for U.S. persons the benefits of reductions in source-country tax on their investments in that country.

Despite the protections provided by the limitation on benefits provisions, there may be countries with which a tax treaty is not appropriate because of the possibility of abuse. With other countries there simply may not be the type of cross-border tax issues that are best resolved by treaty.

For example, we generally do not conclude tax treaties with jurisdictions that do not impose significant income taxes, because there is little possibility of the double taxation of income in the cross-border context that tax treaties are designed to address; with such jurisdictions, an agreement focused on the exchange of tax information can be very valuable in furthering the goal of reducing U.S. tax evasion.

The situation is more complex when a country adopts a special preferential regime

for certain parts of the economy that is different from the rules generally applicable to the country's residents. In those cases, the residents benefiting from the preferential regime do not face potential double taxation and so should not be entitled to the reductions in U.S. withholding taxes accorded by a tax treaty, while a treaty relationship might be useful and appropriate in order to avoid double taxation in the case of the residents who do not receive the benefit of the preferential regime. Accordingly, in some cases we have tax treaty relationships that carve out certain categories of residents and activities from the benefits of the treaty. In other cases, we have determined that economic relations with the relevant country were such that the potential gains from a tax treaty were not sufficient to outweigh the risk of abuse, and have therefore decided against entering into a tax treaty relationship (or have terminated an existing relationship).

Prospective treaty partners must evidence a clear understanding of what their obligations would be under the treaty, including those with respect to information exchange, and must demonstrate that they would be able to fulfill those obligations. Sometimes a potential treaty partner is unable to do so. In other cases we may feel that a tax treaty is inappropriate because the potential treaty partner is not willing to agree to particular treaty provisions that are needed in order to address real tax problems that have been identified by U.S. businesses operating there.

Lesser developed and newly emerging economies, for which capital and trade flows with the United States are often disproportionate or virtually one way, may be reluctant to agree to the reductions in source-country withholding taxes preferred by the United States because of concerns about the short-term effects on their tax revenues. These countries have two somewhat conflicting objectives. They need to reduce barriers to investment, which is the engine of development and growth, and reducing source-country withholding taxes reduces a significant barrier to inward investment. On the other hand, reductions in source-country withholding taxes may reduce tax revenues in the short-term. Because this necessarily involves the other country's judgment regarding the level of withholding taxes that will best balance these two objectives, our tax treaties with developing countries often provide for higher maximum rates of source-country tax than is the U.S. preferred position. Such a treaty nevertheless provides benefits to taxpayers by establishing a stable framework for taxation. Moreover, having an agreement in place makes it easier to agree to further reductions in source-country withholding taxes in the future. It is important to recognize that even where the current capital and trade flows between two treaty countries are disproportionate, conclusion of a tax treaty is not a zero-sum exercise. The goal of the tax treaty is to increase the amount and efficiency of economic activity, so that the situation of each party is improved.

For a country like the United States that has significant amounts of both inbound and outbound investment, treaty reductions in source-country withholding taxes do not have the same one-directional impact on tax revenues, even looking just at the short-term effects. Reductions in withholding tax imposed by the source country on payments made to foreign investors represent a short-term static reduction in source-country tax revenues. However, reductions in foreign withholding taxes borne by residents on payments received with respect to foreign investments represent an increase in tax revenues because of the corresponding reduction in the foreign tax credits that otherwise would offset the residents' domestic tax liabilities. Thus, the reciprocal reductions in source-country withholding taxes accomplished by treaty will have offsetting effects on tax revenues even in the short term.

More importantly, looking beyond any net short-term effect on tax liabilities, an income tax treaty is a negotiated agreement under which both countries expect to be better off in the long run. These long-term economic benefits far outweigh any net short-term static effects on tax liabilities. Securing the reduction or elimination of foreign withholding taxes imposed on U.S. investors abroad can reduce their costs and improve their competitiveness in connection with international business opportunities. Reduction or elimination of the U.S. withholding tax imposed on foreign investors in the United States may encourage inbound investment, and increased investment in the United States translates to more jobs, greater productivity and higher wage rates. The tax treaty as a whole creates greater

certainty and provides a more stable environment for foreign investment. The agreed allocation of taxing rights between the two countries reduces cross-border impediments to the bilateral flow of capital, thereby allowing companies and individuals to more effectively locate their operations in such a way that their investments are as productive as possible. This increased productivity will benefit both countries' economies. The administrative provisions of the tax treaty provide for cooperation between the two countries, which will help reduce the costs of tax administration and improve tax compliance.

Discussion of Proposed New Treaties and Protocols

I now would like to discuss the two agreements that have been transmitted for the Senate's consideration. We have submitted Technical Explanations of each agreement that contain detailed discussions of the provisions of each treaty and protocol. These Technical Explanations serve as an official guide to each agreement.

Japan

The proposed Convention and Protocol with Japan was signed in Washington on November 6, 2003. The Convention and Protocol are accompanied by an exchange of diplomatic notes, also dated November 6, 2003. The Convention, Protocol and notes replace the existing U.S.-Japan tax treaty, which was signed in 1971.

Because the existing treaty dates back to 1971, it does not reflect the changes in economic relations between the two countries that have taken place over the last thirty years. Today, the trade and investment relationship between the United States and Japan, the world's two largest economies, is critical to creating economic growth throughout the world.
The proposed new treaty significantly reduces existing tax-related barriers to trade and investment between Japan and the United States. Reducing these barriers will help to foster still-closer economic ties between the two countries, enhancing the competitiveness of both countries' businesses and creating new opportunities for trade and investment.

The existing treaty also is inconsistent in many respects with U.S. tax treaty policy. The proposed new treaty brings the treaty relationship into much closer conformity with U.S. policy and generally modernizes the agreement in a manner consistent with other recent treaties. At the same time, several key provisions of the new treaty represent "firsts" for Japan. The evolution embodied in this agreement may very well provide important precedents for many countries in the region that look to Japan for guidance and leadership in this regard.

Perhaps the most dramatic advances in the proposed new treaty are reflected in the reciprocal reductions in source-country withholding taxes on income from cross-border investments. The existing treaty sets maximum rates for withholding taxes on cross-border interest, royalty and dividend payments that are much higher than the rates reflected in the U.S. model tax treaty and provided in most U.S. tax treaties with developed countries. The new treaty substantially lowers these maximum withholding tax rates, bringing the limits in line with U.S. preferred tax treaty provisions. The maximum rates of source-country withholding tax provided in the new treaty are as low as, and in many cases significantly lower than, the rates provided for in any other tax treaty entered into by Japan. These important reductions in source-country withholding tax agreed in this new treaty reflect the commitment of both governments to facilitating cross-border investment.

In today's knowledge-driven economy, intangible property developed in the United States, such as trademarks, industrial processes or know-how, is used around the world. Given the importance of the cross-border use of intangibles between the United States and Japan, a primary objective from the U.S. perspective in negotiating a new tax treaty with Japan was to overhaul the existing rules for the treatment of cross-border income from intangible property. This goal is achieved in the proposed new treaty through the complete elimination of source-country

withholding taxes on royalties. This is the first treaty in which Japan has agreed to eliminate source-country withholding taxes on royalties.

The proposed new treaty is a major change from the existing treaty, which allows the source country to impose a 10 percent withholding tax on cross-border royalties. The gross-basis taxation provided for under the existing treaty is particularly likely to lead to excessive taxation in the case of royalties because the developer of the licensed intangible who receives the royalty payments typically incurs substantial expenses, through research and development or marketing. The existing treaty's 10-percent withholding tax imposed on gross royalties can represent a very high effective rate of source-country tax on net income when the expenses associated with such income are considered. In addition, because withholding taxes can be imposed on cross-border payments where the taxpayer has no presence in the source country, the existing treaty's allowance of such taxes on royalties created a significant disparity in treatment between royalty income and services and other income. This has been particularly problematic as the line between the types of income is not always clear.

With the elimination of source-country royalty withholding taxes provided for in the proposed new treaty, royalties will be taxed exclusively by the country of residence on a net basis in the same manner as other business profits. This eliminates the excessive taxation that can occur under the existing treaty. Moreover, treating royalties in the same manner as business profits removes the disparity in treatment between royalty income and services and other income and therefore eliminates what has been a significant source of dispute and potential double taxation for U.S. taxpayers under the existing treaty. As a final note, this change in the U.S.-Japan treaty relationship may well have positive effects for other U.S. treaty negotiations. Japan's historic policy of retaining its right to impose withholding tax on royalties in its tax treaties has encouraged other countries to do the same. The change in this policy reflected in the new treaty may serve as an impetus to other countries to consider agreeing by treaty to greater reductions in source-country withholding taxes on royalties.

The proposed new treaty also reflects significant improvements in the rules regarding cross-border interest payments. The existing treaty provides for a maximum withholding tax rate of 10 percent for all interest payments other than a narrow class of interest paid to certain government entities. The new treaty includes provisions eliminating source-country withholding taxes for significant categories of interest. The most important of these is the elimination of source-country withholding tax for interest earned by financial institutions. Due to the highly-leveraged nature of financial institutions, imposition of a withholding tax on interest received by such enterprises could result in taxation that actually exceeds the net income from the transaction. The new treaty will eliminate this potential for excessive taxation, with cross-border interest earned by financial institutions taxed exclusively by the residence country on a net basis. The new treaty also provides for the elimination of source-country withholding taxes in the case of interest received by the two governments, interest received in connection with sales on credit, and interest earned by pension funds. This elimination of source-country withholding taxes on income earned by tax-exempt pension funds ensures that the assets expected to accumulate tax-free to fund retirement benefits are not reduced by foreign taxes; a withholding tax in this situation would be particularly burdensome because there is no practical mechanism for providing individual pension beneficiaries with a foreign tax credit for withholding taxes that were imposed on investment income years before the retiree receives pension distributions. These exemptions from source-country withholding tax for interest provided in the new treaty are broader than in any other Japanese tax treaty.

In addition, the proposed new treaty significantly reduces source-country withholding taxes with respect to all types of cross-border dividends. Under the existing treaty, direct investment dividends (that is, dividends paid to companies that own at least 10 percent of the stock of the paying company) generally may be taxed by the source country at a maximum rate of 10 percent and portfolio dividends may be taxed at a maximum rate of 15 percent. The new treaty reduces the maximum rates of source-country withholding tax to 5 percent for direct investment dividends and 10 percent for portfolio dividends. The new treaty also provides for the elimination of source-country withholding taxes on certain

intercompany dividends where the dividend is received by a company that owns more than fifty percent of the voting stock of the company paying the dividend. This provision is similar to provisions included in the U.S. treaties with the United Kingdom, Australia, and Mexico.

The elimination of withholding taxes on this category of intercompany dividends is substantially narrower than provisions in other Japanese treaties. In addition, the new treaty includes a provision that eliminates source-country withholding taxes on dividends paid to pension funds, which parallels the treatment of interest paid to pension funds.

Treasury believes that this provision eliminating source-country withholding taxes on certain intercompany dividends is appropriate in light of our overall treaty policy of reducing tax barriers to cross-border investment and in the context of this important treaty relationship. As I have testified previously, the elimination of source-country taxation of dividends is something that is to be considered only on a case-by-case basis. It is not the U.S. model position because we do not believe that it is appropriate to agree to such an exemption in every treaty. Consideration of such a provision in a treaty is appropriate only if the treaty contains anti-treaty-shopping rules that meet the highest standards and the information exchange provision of the treaty is sufficient to allow us to confirm that the requirements for entitlement to this benefit are satisfied. Strict protections against treaty shopping are particularly important when the elimination of withholding taxes on intercompany dividends is included in relatively few U.S. treaties. In addition to these prerequisites, the overall balance of the treaty must be considered.

These conditions and considerations all are met in the case of the proposed new treaty with Japan. The new treaty includes the comprehensive anti-treaty-shopping provisions sought by the United States, provisions that are not contained in the existing treaty. The new treaty includes exchange of information provisions comparable to those in the U.S. model treaty. In this regard, Japan recently enacted domestic legislation to ensure that it can obtain and exchange information pursuant to a tax treaty even in cases where it does not need the particular information for its own tax purposes.

The United States and U.S. taxpayers benefit significantly both from this provision in the new agreement and from the treaty overall. The elimination of source-country withholding taxes on intercompany dividends provides reciprocal benefits because Japan and the United States both have dividend withholding taxes and there are substantial dividend flows going in both directions. U.S. companies that are in an excess foreign tax credit position will be able to keep every extra dollar they receive if the dividends they repatriate to the United States are free of Japanese withholding tax. The treaty as a whole reflects dramatic reductions in source-country withholding taxes relative to the existing treaty. The elimination of withholding taxes on royalties and certain interest was a key objective for the United States; while these provisions secured in this new treaty are consistent with U.S. tax treaty policy, they are an unprecedented departure from historic Japanese tax treaty policy.

Another important change reflected in the proposed new treaty is the addition of an article providing for the elimination of source-country withholding taxes on "other income", which include types of financial services income that under the existing treaty could have been subject to gross-basis tax by the source country. In particular, the Protocol confirms that securities lending fees, guarantee fees, and commitment fees generally will not be subject to source-country withholding tax and rather will be taxable in the same manner as other business profits.

The proposed new treaty provides that the United States generally will not impose the excise tax on insurance policies issued by foreign insurers if the premiums on such policies are derived by a Japanese enterprise. This provision, however, is subject to the anti-abuse rule that denies the exemption if the Japanese insurance company were to enter into reinsurance arrangements with a foreign insurance company that is not itself eligible for such an exemption.

Another significant modernization reflected in the proposed new treaty is the

inclusion of specific rules regarding the application of treaty provisions in the case of investments in one country made by residents of the other country through partnerships and other flow-through entities. These rules coordinate the domestic law rules of Japan and the United States in this area in order to provide for certainty in results for cross-border businesses operated in partnership form.

In the case of shipping income, the proposed new treaty provides for exclusive residence-country taxation of profits from the operation in international traffic of ships or aircraft. This elimination of source-country tax covers profits from the rental of ships and aircraft on a full basis; it also covers profits from rentals on a bareboat basis if the rental income is incidental to profits from the operation of ships or aircraft in international traffic. In addition, the new treaty provides an exemption from source-country tax for all income from the use, maintenance or rental of containers used in international traffic.

The proposed new treaty generally provides for exclusive residence-country taxation of gains with narrow exceptions, which is generally consistent with U.S. tax treaty preferences but is a departure from the source-country taxation of gains that is provided for in recent Japanese treaties. The new treaty provides for source-country taxation of share gains in two circumstances. First, the new treaty includes a rule similar to that in U.S. domestic law under which gains from the sale of shares or other interests in an entity investing in real estate may be taxed by the country in which the real estate is located. Second, it contains a narrow rule dealing with gains on stock in restructured financial institutions that was included at the request of Japan. Under this rule, the source country may tax gains on stock of a financial institution if the financial institution had received substantial financial assistance from the government under rules relating to distressed financial institutions, the stock was purchased from the government, and the stock is sold within five years of such assistance. Under a very broad grandfather rule, this provision does not apply to any stock held by an investor who made an investment in such a financial institution prior to the entry into force of the new treaty including any additional stock in the financial institution that the investor acquires subsequently.

Like the existing treaty, the proposed new treaty provides that pensions and social security benefits may be taxed only by the residence country. The new treaty also provides rules regarding the allocation of taxing rights with respect to compensation earned in the form of employee stock options.

The proposed new treaty provides rules governing income earned by entertainers and sportsmen, corporate directors, government employees, and students that are consistent with the rules of the U.S. model treaty. The new treaty continues and improves a host-country exemption for income earned by teachers that is found in the existing treaty, although not in the U.S. model.

The proposed new treaty contains a comprehensive limitation on benefits article, which provides detailed rules designed to deny "treaty shoppers" the benefits of the treaty. These rules, which were not contained in the existing treaty and which have not been included in this form in other Japanese tax treaties, are comparable to the rules contained in recent U.S. treaties.

At the request of Japan, the proposed new treaty includes an additional limit on the availability of treaty benefits obtained in connection with certain back-to-back transactions involving dividends, interest, royalties or other income. This provision is substantially narrower than the "conduit arrangement" language found in the 2003 treaty with the United Kingdom. It is intended to address abusive transactions involving income that flows to a third-country resident. Japanese domestic law does not provide sufficient protection against these abusive transactions. The stricter protections against this type of abuse that are provided under U.S. domestic law will continue to apply.

The proposed new treaty provides relief from double taxation in a manner consistent with the U.S. model. The new treaty also includes a re-sourcing rule to ensure that a U.S. resident can obtain a U.S. foreign tax credit for Japanese taxes paid when the treaty assigns to Japan primary taxing rights over an item of gross income. A comparable rule applies for purposes of the Japanese foreign tax credit.

The proposed new treaty provides for non-discriminatory treatment (i.e., national treatment) by one country to residents and nationals of the other. Also included in the new treaty are rules necessary for administering the treaty, including rules for the resolution of disputes under the treaty. The information exchange provisions of the new treaty generally follow the U.S. model and make clear that Japan will provide U.S. tax officials such information as is relevant to carry out the provisions of the treaty and the domestic tax laws of the United States. Inclusion of this U.S. model provision was made possible by a recent change in Japanese law.

Sri Lanka

The United States does not currently have an income tax treaty with Sri Lanka. The proposed income tax Convention with Sri Lanka was signed in Colombo on March 14, 1985 but was not acted on by the Senate at that time because changes made to U.S. international tax rules by the Tax Reform Act of 1986 necessitated some modifications to the agreement. The proposed Protocol, which was signed on September 20, 2002, amends the 1985 Convention to reflect changes in domestic law since 1985 as well as developments in U.S. tax treaty policy and includes modifications that better reflect U.S. tax treaty preferences. We are requesting the Committee to report favorably on both the 1985 Convention and the 2002 Protocol.

The proposed new treaty generally follows the pattern of the U.S. model treaty, while incorporating some provisions found in other U.S. treaties with developing countries. The maximum rates of source-country withholding taxes on investment income provided in the proposed treaty are generally equal to or lower than the maximum rates provided in other U.S. treaties with developing countries (and some developed countries).

The proposed treaty generally provides a maximum source-country withholding tax rate on dividends of 15 percent. Special rules consistent with those in the U.S. model treaty apply to certain dividends paid by a U.S. real estate investment trust. The proposed treaty provides a maximum source-country withholding tax rate on interest of 10 percent. This source-country tax is eliminated in the case of interest paid by one of the two governments or received by one of the two governments or one of the central banks.

Under the proposed treaty, royalties may be subject to source-country withholding taxes at a maximum rate of 10 percent. As in many treaties with developing countries, the royalties article also covers rents with respect to tangible personal property; in the case of such rents, however, the maximum withholding tax rate is 5 percent. These rules in the proposed treaty do not apply to rental income with respect to the lease of containers, ships or aircraft, which is instead covered by the specific rules in the shipping article.

The rules in the proposed treaty relating to income from shipping and air transport are complicated in terms of drafting, but produce results that in most cases are consistent with many recent U.S. tax treaties. First and simplest, under the proposed treaty income derived from the rental of containers used in international traffic is taxable only in the country of residence and not in the source country. Exclusive residence-country taxation of such income is the preferred U.S. position reflected in the U.S. model treaty. Second, the proposed treaty provides that income derived from the international operation of aircraft also is taxable only in the country of residence. This rule eliminating source-country tax covers income derived from aircraft leases on a full basis as well as profits from the rental of aircraft on a bareboat basis if the aircraft are operated in international traffic by the lessee or if the lease is incidental to other profits from the operation of aircraft. Third, the rules in the treaty provide for some source-country taxation of income from the operation and rental of ships, but not to exceed the source-country tax that may be imposed under any of Sri Lanka's other treaties. Sri Lanka has entered into two treaties that eliminate source-country tax on income from the operation of ships and has confirmed through diplomatic note that this exemption from source-country tax will apply in the case of the United States as well.

The proposed treaty provides the basic tax treaty rule that business profits of a resident of one of the treaty countries generally may be taxed in the other country

only when such profits are attributable to a permanent establishment located in that other country. The rules in the proposed treaty permit broader host-country taxation than is provided for in the U.S. model treaty. In this regard, the definition of permanent establishment in the proposed treaty is somewhat broader than the definition in the U.S. model, which lowers the threshold level of activity required for imposition of host-country tax. This permanent establishment definition is consistent with other U.S. treaties with developing countries. In addition, the proposed treaty provides that certain profits that are not attributable to the permanent establishment may be taxed in the host state if they arise from business activities carried on in the host state that are similar to those carried on through the permanent establishment. These rules are quite similar to rules found in our tax treaties with other developing countries.

The proposed treaty's rules for taxation of income from personal services similarly are consistent with our recent treaties with developing countries. Under the proposed treaty, income earned through independent personal services may be taxed in the host country if they are performed through a fixed base or if the individual performing the services was in the host country for more than 183 days in any 12-month period. The proposed treaty provides rules governing income earned by entertainers and sportsmen, corporate directors and government employees that are broadly consistent with the rules of the U.S. model treaty. The proposed treaty also includes a limited exemption from source country taxation of students.

The proposed treaty contains a comprehensive limitation on benefits article, which provides detailed rules designed to deny "treaty shoppers" the benefits of the treaty. These rules are comparable to the rules contained in the U.S. model and recent U.S. treaties.

The proposed treaty also sets out the manner in which each country will relieve double taxation. Both the United States and Sri Lanka will provide such relief through the foreign tax credit mechanism, including a deemed paid credit for indirect taxes paid by subsidiary companies.

The proposed treaty provides for non-discriminatory treatment (i.e., national treatment) by one country to residents and nationals of the other. Also included in the proposed treaty are rules necessary for administering the treaty, including rules for the resolution of disputes under the treaty.

The proposed treaty includes an exchange of information provision that generally follows the U.S. model. Under these provisions, Sri Lanka will provide U.S. tax officials such information as is relevant to carry out the provisions of the treaty and the domestic tax laws of the United States. Sri Lanka has confirmed through diplomatic note its ability to obtain and exchange key information relevant for tax purposes. The information that may be exchanged includes information held by financial institutions, nominees or persons acting in an agency or fiduciary capacity.

Treaty Program Priorities

We continue to maintain a very active calendar of tax treaty negotiations. We currently are in ongoing negotiations with Bangladesh, Canada, Chile, Hungary, Iceland and Korea. We also have substantially completed work with the Netherlands, France and Barbados and look forward to the conclusion of these new agreements.

With respect to future negotiations, we expect to begin discussions soon with Germany and Norway. Another key priority is updating the few remaining treaties that provide for low withholding tax rates but do not include the limitation on benefits provisions needed to protect against the possibility of treaty shopping. Also a priority is entering into new treaties with the former Soviet republics that are still covered by the old U.S.S.R. treaty (which does not include an adequate exchange of information provision). We also are focused on continuing to expand our treaty network by entering into new tax treaty relationships with countries that have the potential to be important trading partners in the future.

Significant resources have been devoted in recent years to the negotiation of new tax treaties with Japan and the United Kingdom, two major trade and investment partners for the United States and two of our oldest tax treaties. With the completion of these important negotiations, we believe that it would be appropriate to update the U.S. model treaty to reflect our negotiating experiences since 1996. A new model will help facilitate the negotiations we expect to begin in the near future. We look forward to working with the staffs of the Senate Foreign Relations Committee and Joint Committee on Taxation on this project.

Conclusion

Let me conclude by again thanking the Committee for its continuing interest in the tax treaty program, and the Members and staff for devoting the time and attention to the review of these new agreements. We appreciate the assistance and cooperation of the staffs of this Committee and of the Joint Committee on Taxation in the tax treaty process.

We urge the Committee to take prompt and favorable action on the agreements before you today. Such action will help to reduce barriers to cross-border trade and investment by further strengthening our economic relations with a country that has been a significant economic and political partner for many years and by expanding our economic relations with an important trading partner in the developing world.

Related Documents:

- Technical Explanation: Japan Treaty
- Technical Explanation: Sri Lanka Protocol

DEPARTMENT OF THE TREASURY TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF JAPAN FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL GAINS, SIGNED AT WASHINGTON ON NOVEMBER 6, 2003

This is a technical explanation of the Convention between the Government of the United States of America and the Government of Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, signed at Washington on November 6, 2003 (the "Convention"), and the Protocol also signed at Washington on November 6, 2003, which forms an integral part thereto (the "Protocol"). In connection with the negotiation of the Convention, the delegations of the United States and Japan developed and agreed upon an exchange of Diplomatic Notes (the "Notes"). The Notes constitute an agreement between the two governments that shall enter into force at the same time as the entry into force of the Convention. The Notes are intended to give guidance both to the taxpayers and to the tax authorities of the Contracting States in interpreting the Convention. The Notes and Protocol are discussed below in connection with relevant provisions of the Convention.

References are made to the Convention between the Government of the United States of America and the Government of Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, signed at Tokyo on March 8, 1971 (the "prior Convention"). The Convention and Protocol replace the prior Convention.

Negotiations took into account the U.S. Treasury Department's current tax treaty policy and the Treasury Department's Model Income Tax Convention, published on September 20, 1996 (the "U.S. Model"). Negotiations also took into account the Model Tax Convention on Income and on Capital, published by the Organization for Economic Cooperation and Development, as updated in January 2003 (the "OECD Model"), and recent tax treaties concluded by both countries.

The Technical Explanation is an official guide to the Convention. It reflects the policies behind particular Convention provisions, as well as understandings reached with respect to the application and interpretation of the Convention. While the Convention does not include subject matter headings or titles for the Articles, such headings are included in the Technical Explanation for ease of use. The headings included generally correspond to headings of analogous articles of the U.S. Model where possible, and it is not intended that any legal effect be given to the headings or to the fact of their inclusion in the Technical Explanation. References in the Technical Explanation to "he" or "his" should be read to mean "he or she" or "his or her."

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DEPARTMENT OF THE TREASURY TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME SIGNED AT COLOMBO MARCH 14, 1985, AS AMENDED BY A PROTOCOL SIGNED AT WASHINGTON ON SEPTEMBER 20, 2002

This is a Technical Explanation of the Convention between the Government of the United States of America and the Government of the Democratic Socialist Republic of Sri Lanka for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income Signed at Colombo March 14, 1985 (the "Convention"). The Convention was amended by a Protocol signed on September 20, 2002 (the "Protocol"), which was accompanied by an explanatory Exchange of Notes (the "Notes").

Negotiations with respect to the Protocol took into account the U.S. Treasury Department's current tax treaty policy and the U.S. Treasury Department's Model Income Tax Convention published September 20, 1996 (the "U.S. Model"). Negotiations also took into account the Model Income Tax Convention on Income and on Capital, published by the Organization for Economic Cooperation and Development (the "OECD Model"), the United Nations Model Double Taxation Convention Between Developed and Developing Countries (the "UN Model"), and recent tax treaties concluded by both countries.

The Technical Explanation is an official guide to the Convention. It reflects the policies behind particular Convention provisions, as well as understandings reached with respect to the application and interpretation of the Convention.

References in the Technical Explanation to "he" or "his" should be read to mean "he or she" and "his or her."

Article 1 (Personal Scope)

Paragraph 1

Paragraph 1 of Article 1 provides that the Convention applies to residents of the United States or Sri Lanka, except where the terms of the Convention provide otherwise. Under Article 4 (Resident) a person is generally treated as a resident of a Contracting State if that person is, under the laws of that State, liable to tax therein by reason of his domicile or other similar criteria. If, however, a person is considered a resident of both Contracting States, a single state of residence (or no state of residence) is assigned under Article 4. This determination generally governs for purposes of the Convention.

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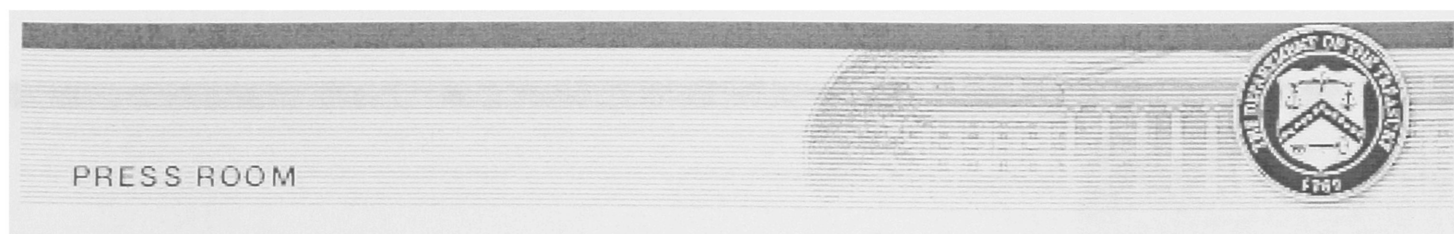

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 25, 2004
JS-1192

Treasury and IRS Issue Guidance on "Swaps"

Today the Treasury Department and the Internal Revenue Service issued proposed regulations regarding the taxation of contingent nonperiodic payments with respect to notional principal contracts (NPCs). These contracts consist mainly of those transactions referred to in the financial marketplace as "swaps."

Existing final regulations state that the income or deduction for a nonperiodic payment must be recognized by a party to the NPC in an economic manner over the full term of the NPC. The existing regulations implement this principle for fixed nonperiodic payments, but do not contain any explicit rules or examples for significant contingent nonperiodic payments, which are included in some NPCs. Some taxpayers have taken the position that, regardless of economic expectations, a party to a NPC need not recognize any income with respect to a contingent nonperiodic payment before the amount of the payment is finally fixed (a "wait and see" approach). Such a wait-and-see approach generally postpones the recognition of taxable income and may let a taxpayer choose to enjoy winning positions as sources of capital gain but to garner ordinary deductions from any losers.

The proposed regulations set forth a pair of more economic methods of accounting for significant contingent nonperiodic payments. First, a generally applicable method requires a taxpayer to estimate the amount of any contingent future payment and, on the basis of that estimate, to recognize an appropriate portion in the each taxable year. Additional estimations must take place every year, and the taxpayer must include or deduct a "true-up" adjustment each year to the extent that the more up-to-date estimate indicates that prior accruals were wrong.

Second, for most NPCs, the taxpayer may instead elect to mark the NPCs to market. That is, the taxpayer may choose to recognize income or deduction at the end of each year, based on the extent to which the NPCs changed in value during the year. Because many taxpayers are already required to mark their derivative positions to market for financial statement purposes, taxpayers should find this method particularly easy to use.

Related Documents:

- The text of the proposed regulations

FROM THE OFFICE OF PUBLIC AFFAIRS

February 25, 2004
2004-3-2-17-28-54-11523

U.S. International Reserve Position

The Treasury Department today released U.S. reserve assets data for the latest week. As indicated in this table, U.S. reserve assets totaled $85,437 million as of the end of that week, compared to $86,609 million as of the end of the prior week.

I. Official U.S. Reserve Assets *(in US millions)*

	February 13, 2003			February 20, 2004		
TOTAL		86,609			85,437	
1. Foreign Currency Reserves [1]	Euro	Yen	TOTAL	Euro	Yen	TOTAL
a. Securities	8,617	14,896	23,513	8,669	14,453	23,123
Of which, issuer headquartered in the U.S.			0			0
b. Total deposits with:						
b.i. Other central banks and BIS	13,944	2,993	16,937	13,566	2,904	16,470
b.ii. Banks headquartered in the U.S.			0			0
b.ii. Of which, banks located abroad			0			0
b.iii. Banks headquartered outside the U.S.			0			0
b.iii. Of which, banks located in the U.S.			0			0
2. IMF Reserve Position [2]			22,288			22,088
3. Special Drawing Rights (SDRs) [2]			12,829			12,713
4. Gold Stock [3]			11,043			11,043
5. Other Reserve Assets			0			0

II. Predetermined Short-Term Drains on Foreign Currency Assets

	February 13, 2003			February 20, 2004		
	Euro	Yen	TOTAL	Euro	Yen	TOTAL
1. Foreign currency loans and securities			0			0

2.a. Short positions	0	0
2.b. Long positions	0	0
3. Other	0	0

III. Contingent Short-Term Net Drains on Foreign Currency Assets

	February 13, 2003			February 20, 2004		
	Euro	**Yen**	**TOTAL**	**Euro**	**Yen**	**TOTAL**
1. Contingent liabilities in foreign currency			0			0
1.a. Collateral guarantees on debt due within 1 year						
1.b. Other contingent liabilities						
2. Foreign currency securities with embedded options			0			0
3. Undrawn, unconditional credit lines			0			0
3.a. With other central banks						
3.b. With banks and other financial institutions Headquartered in the U.S.						
3.c. With banks and other financial institutions Headquartered outside the U.S.						
4. Aggregate short and long positions of options in foreign Currencies vis-à-vis the U.S. dollar			0			0
4.a. Short positions						
.a.1. Bought puts						
.a.2. Written calls						
b. Long positions						
b.1. Bought calls						
b.2. Written puts						

Notes:

cludes holdings of the Treasury's Exchange Stabilization Fund (ESF) and the Federal Reserve's System Open Market Account MA), valued at current market exchange rates. Foreign currency holdings listed as securities reflect marked-to-market values, and

Reserves for the prior week are final.

2/ The items, "2. IMF Reserve Position" and "3. Special Drawing Rights (SDRs)," are based on data provided by the IMF and are valued in dollar terms at the official SDR/dollar exchange rate for the reporting date. The entries for the latest week reflect any necessary adjustments, including revaluation, by the U.S. Treasury to IMF data for the prior month end.

3/ Gold stock is valued monthly at $42.2222 per fine troy ounce.

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 25, 2004
JS-1193

Treasury and IRS Shut Down
Aggressive Executive Stock Transaction

Today, the Treasury Department and the IRS issued a revenue ruling that would shut down an aggressive transaction involving the exercise of stock options by corporate insiders using debt financing provided by the corporation.

In these transactions, typically the corporate insider will exercise options he or she holds by giving the company a promissory note. If the value of the stock later falls below the face amount of the note, the company may agree to reduce the insider's debt. Certain individuals have claimed that this debt reduction does not result in taxable income.

Revenue Ruling 2004-37 provides that reduction of debt in these circumstances does result in taxable income to the insider. By forgiving part of the purchase price, the company has increased the amount of stock that the insider has received without paying for the stock. If the stock was not paid for by the insider, the insider will be treated as receiving compensation.

Acting Assistant Secretary for Tax Policy Greg Jenner stated, "Once again, we have made it clear that everyone has to play by the same rules. A corporate insider whose compensation is increased because the company reduces the purchase price on stock the insider has already purchased must pay tax on that increased compensation."

The ruling also provides that a reduction in the interest rate under the note, or a change in the note so that the executive no longer has personal liability, also would result in compensation income.

Related Documents:

- The text of Revenue Ruling 2004-37

Part I

Section 83.--Property Transferred in Connection with Performance of Services

26 C.F.R. 1.83-4: Special rules.
(Also §§ 108, 3121, 3306, 3401, 1.1001-3)

Rev. Rul. 2004-37

ISSUE

If an employee issued a recourse note to his or her employer in satisfaction of the exercise price of an option to acquire the employer's stock and the employer and employee subsequently agree to reduce the stated principal amount of the note, does the employee recognize compensation income under § 83 of the Internal Revenue Code?

FACTS

In Year 1, Employer, a corporation, grants a nontransferable, nonstatutory option to its Employee to purchase 1,000 shares of Employer common stock at an exercise price of $75 per share, the fair market value of a share of Employer stock at the time the option is granted. Employee may exercise the option only during employment with Employer or within 90 days after cessation of employment.

On January 1 of Year 2, when the fair market value of 1,000 shares of Employer stock is $100,000, Employee exercises the option and purchases 1,000 shares of Employer stock in exchange for a nontransferable recourse note ("Note") secured by the stock Employee receives on the exercise of the option. The Note has a stated principal amount of $75,000, which is payable at maturity on December 31 of Year 11.

The Note also provides for payments of interest on December 31 of each year the Note is outstanding. The interest rate is one-year LIBOR (determined as of January 1 of each year the Note is outstanding) plus 25 basis points. The interest rate on the Note is not less than the appropriate applicable Federal rate (AFR) on the date the Note is issued. The stock is not subject to a substantial risk of forfeiture within the meaning of § 83(c).

In Year 2, Employee includes $25,000 as compensation income under § 83(a). Employer reports $25,000 of compensation income on the Form W-2 issued to Employee for Year 2 and claims a corresponding deduction in Year 2 under § 83(h).

In Years 2 and 3, Employee makes the required interest payments under the Note. On January 1 of Year 4, the fair market value of the Employer stock has declined to $50,000 and Employer and Employee agree to reduce the stated principal amount of the Note from $75,000 to $50,000. The interest rate on the Note is not less than the appropriate AFR on the date the Note is modified.

LAW

Section 83(a) provides that if, in connection with the performance of services, property is transferred to any person other than the person for whom such services are performed, the excess of the fair market value of the property at the first time that the rights to the property are either transferable or not subject to a substantial risk of forfeiture ("substantially vested"), whichever occurs earlier, over the amount paid for the property is included in the gross income of the service provider in the first taxable year in which the rights to the property are substantially vested.

Section 83(e)(3) provides that § 83 does not apply to the transfer of an option without a readily ascertainable fair market value.

Section 83(h) provides that, in the case of a transfer of property to which § 83 applies, the person for whom were performed the services in connection with which the property was transferred is allowed a deduction in an amount equal to the amount

included under § 83(a), (b), or (d)(2) in the gross income of the person who performed the services. Such deduction is allowed for the taxable year of such person in which or with which ends the taxable year in which such amount is included in the gross income of the person who performed such services.

Section 1.83-3(a)(1) of the Income Tax Regulations provides that a "transfer" of property occurs when a person acquires a beneficial ownership interest in the property. A person acquires a beneficial ownership interest in property when he or she has been transferred both the right to share in an increase in the value of the property and the obligation to share in the risk of loss in its value. Whether a transfer has in fact occurred is based on all the facts and circumstances.

Section 1.83-3(g) provides that the term "amount paid" refers to the value of any money or property paid for the transfer of property to which § 83 applies. For this purpose, value does not include any stated or unstated interest.

Section 1.83-4(c) provides that, if an indebtedness that has been treated as an "amount paid" for purposes of § 83 is subsequently cancelled, forgiven, or satisfied for an amount less than the amount of such indebtedness, the amount that is not, in fact, paid is includible in the gross income of the service provider for the taxable year in which such cancellation, forgiveness, or satisfaction occurs.

Section 1.83-7(a) provides that the grant of a nonqualified stock option is taxable to the extent that the option has a readily ascertainable fair market value, determined in accordance with § 1.83-7(b). Under § 1.83-7(b), an option that is not traded on an established market does not have a readily ascertainable value at the time of grant unless certain specific conditions are all satisfied (including the option being transferable, the option not being subject to a condition that has a significant effect on the fair market value of the option, and the fair market value of the option privilege being readily ascertainable). Under § 1.83-7(a), if the option does not have a readily ascertainable value at the time of grant, §§ 83(a) and 83(b) apply at such time as the

option is exercised or otherwise disposed of, even though the fair market value of such option may have become readily ascertainable before such time.

Section 61(a)(12) provides that, in general, gross income includes income from the discharge of indebtedness.

Section 108(a)(1)(B) provides an exclusion from gross income for any amount that would be includible in gross income by reason of the discharge of indebtedness of the taxpayer if the discharge occurs when the taxpayer is insolvent.

Under § 108(e)(5), for solvent and non-bankrupt taxpayers, if debt owed by a purchaser to a seller is reduced, the reduction is a purchase price adjustment and not income from discharge of indebtedness. Under § 108(e)(5)(C), § 108(e)(5) only applies to reductions that, but for the application of § 108(e)(5), would be treated as income to the purchaser from the discharge of indebtedness.

Not every indebtedness that is cancelled results in the debtor realizing gross income by reason of discharge of indebtedness within the meaning of §§ 61(a)(12) and 108(a). "Debt discharge that is only a medium for some other form of payment, such as a gift or salary, is treated as that form of payment, rather than under the debt discharge rules." S. Rep. No. 1035, 96th Cong., 2d Sess. 8 n.6 (1980), 1980-2 C.B. 620, 624 n.6.

Section 1.1001-3 provides rules to determine whether a modification of the terms of a debt instrument results in an exchange of the original debt instrument for a modified instrument that differs materially either in kind or in extent. If the modification results in an exchange, the adequacy of the interest rate on the modified debt instrument generally is retested under the applicable Code section, such as § 483.

Under § 1.1001-3(b), a modification of a debt instrument results in an exchange for purposes of § 1.1001-1(a) if the modification is significant. Under § 1.1001-3(c), a modification means any alteration, including any deletion or addition, in whole or in part, of a legal right or obligation of the issuer or a holder of a debt instrument, whether the alteration is evidenced by an express agreement (oral or written), conduct of the parties,

or otherwise.

Section 1.1001-3(e) provides rules for determining whether a modification is "significant." Under § 1.1001-3(e)(2), a change in the yield of a debt instrument is a significant modification if the yield computed under § 1.1001-3(e)(2)(iii) varies from the annual yield on the unmodified debt instrument (determined as of the date of the modification) by more than the greater of 1/4 of one percent (25 basis points) or 5 percent of the annual yield of the unmodified debt instrument (.05 x annual yield).

Sections 3101 and 3111 impose Federal Insurance Contributions Act (FICA) taxes on "wages," as that term is defined in § 3121(a). FICA taxes consist of the Old-Age, Survivors and Disability Insurance tax (social security tax) and the Hospital Insurance tax (Medicare tax). These taxes are imposed both on the employer under § 3111(a) and (b) and on the employee under § 3101(a) and (b). Section 3102(a) provides that the employee portion of FICA tax must be collected by the employer of the taxpayer by deducting the amount of the tax from the wages as and when paid. Section 31.3102(a)-1(a) of the Employment Tax Regulations provides that the employer is required to collect the tax, notwithstanding that wages are paid in something other than money. The term "wages" is defined in § 3121(a) for FICA purposes as all remuneration for employment including the cash value of all remuneration (including benefits) paid in any medium other than cash, with certain specific exceptions. Section 3121(b) defines "employment" for FICA purposes as any service, of whatever nature, performed by an employee for the person employing him, with certain specific exceptions.

Rules similar to the FICA rules apply with respect to Federal Unemployment Tax Act (FUTA) tax under §§ 3301, 3306(b), and 3306(c).

Section 3402(a), relating to income tax withholding, generally requires every employer making a payment of wages to deduct and withhold upon these wages a tax determined in accordance with prescribed tables or computational procedures. Section

3401(a) provides that "wages" for income tax withholding purposes means all remuneration for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash, with certain specific exceptions. Under § 31.3402(a)-1(c), an employer is required to deduct and withhold income tax notwithstanding that the wages are paid in something other than money (for example, wages paid in stock or bonds) and to pay over the tax in money. If the wages are paid in property other than money, the employer should make necessary arrangements to insure that the amount of the tax required to be withheld is available for payment in money.

Sections 31.3121(a)-1(e), 31.3306(b)-1(e), and 31.3401(a)-1(a)(4) provide that in general the medium in which the remuneration is paid is immaterial. It may be paid in cash or other than in cash. Remuneration paid in any medium other than cash is computed on the basis of the fair market value of such items at the time of payment. Sections 31.3121(a)-1(i), 31.3306(b)-1(i), and 31.3401(a)-1(a)(5) provide that, unless specifically excepted, remuneration for employment constitutes wages even though at the time paid the relationship of employer and employee no longer exists between the person in whose employ the services were performed and the individual who performed the services.

In Rev. Rul. 79-305, 1979-2 C.B. 350, a corporation transferred common stock to an employee subject to a substantial risk of forfeiture. The ruling holds that, under § 83, the fair market value of the stock at the time the risk lapses is includible in the employee's gross income for the year in which risk lapses. The ruling also holds that the fair market value of the stock at the time the risk lapses is wages for purposes of §§ 3121(a), 3306(b), and 3401(a).

ANALYSIS

Under § 1.83-7(b), the option granted to Employee did not have a readily ascertainable fair market value at the time of grant. Therefore, § 83 applies when the

option is exercised and stock is transferred to Employee.

Employee acquired beneficial ownership of the shares of Employer stock in Year 2 because, at that time, Employee acquired both the right to enjoy any increase in the value of the shares and the risk of a decline in the value of the shares. Accordingly, for purposes of § 83, the shares were transferred to Employee in Year 2. Employee's Note, with an issue price of $75,000, constituted the amount paid by Employee for the shares under § 1.83-3(g) in Year 2. Employee included $25,000 in gross income under § 83(a) in Year 2, the excess of the fair market value of Employer stock at the time of transfer over the amount paid.

Under § 1.83-4(c), if an indebtedness that has been treated as an "amount paid" for purposes of § 83 is subsequently cancelled, forgiven, or satisfied for an amount less than the amount of such indebtedness, the amount that is not, in fact, paid is includible in the gross income of the service provider for the taxable year in which such cancellation, forgiveness, or satisfaction occurs. Thus, if the reduction of the stated principal amount of the Note is a cancellation, forgiveness, or satisfaction of the indebtedness for an amount less than the amount of such indebtedness, the reduction of the stated principal amount is a medium for payment of compensation by Employer to Employee, and any income resulting from the reduction is not income to Employee from the discharge of indebtedness subject to the provisions of section 108. Accordingly, the tax consequences of the reduction are governed by § 83 and § 1.83-4(c), and not by § 108(a)(1)(B) or § 108(e)(5).

Whether the reduction of the stated principal amount of the Note is a cancellation, forgiveness, or satisfaction for an amount less than the amount of the Note, and, thus, whether an amount is includible in income under § 1.83-4(c), is determined in accordance with § 1.1001-3. Under § 1.1001-3(e)(2), if a modification to the stated principal amount of a note produces a significant change in the note's yield, the modification is significant. A significant modification results in an exchange of the

unmodified note for the modified note, which, depending on the issue price of the modified note and the adjusted issue price of the unmodified note, may have tax consequences for both the issuer and holder of the note.

In this case, the reduction in the stated principal amount of the Note is a significant modification under § 1.1001-3(e)(2). As a result, there is an exchange of the unmodified Note for the modified Note between Employee and Employer and a satisfaction of the original indebtedness. Under § 1.83-4(c), the amount that is not, in fact, paid, and thus the amount includible as compensation by Employee, is the excess of the adjusted issue price of the unmodified Note over the issue price of the modified Note.

The modified Note has adequate stated interest under § 483. Under § 1273(b)(4), the modified Note has an issue price of $50,000. The adjusted issue price of the unmodified Note is $75,000. See § 1.1275-1(b). As a result, under § 1.83-4(c), Employee recognizes compensation income of $25,000 (the excess of the adjusted issue price of the unmodified Note ($75,000) over the issue price of the modified Note ($50,000)). This amount is recognized in Year 4, the taxable year in which the modification occurred.

HOLDING

If an employee issued a recourse note to his or her employer in satisfaction of the exercise price of an option to acquire the employer's stock and the employer and employee subsequently agree to reduce the stated principal amount of the note, the employee generally recognizes compensation income under § 83 at the time of the reduction. Thus, under the facts described above, Employee recognizes $25,000 of compensation income on January 1 of Year 4 under § 1.83-4(c). If Employer and Employee instead were, for example, to reduce the interest rate on the Note or change the Note from recourse to nonrecourse, that modification also generally would result in

compensation income for Employee.

In addition, the compensation is wages for purposes of FICA, FUTA, and income tax withholding.

DRAFTING INFORMATION

The principal authors of this revenue ruling are Jean M. Casey of the Office of the Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities) and Rebecca Asta of the Associate Chief Counsel (Financial Institutions and Products). For further information regarding § 83, contact Ms. Casey at (202) 622-6030 and for further information regarding § 1.1001-3, contact Ms. Asta at (202) 622-3940 (not toll-free calls).

federal financing bank
WASHINGTON, D.C. 20220
NEWS

FEDERAL FINANCING BANK

2004 PRESS RELEASE

February 2004

Brian Jackson, Chief Financial Officer, Federal Financing Bank (FFB) announced the following activity for the month of February 2004.

FFB holdings of obligations issued, sold or guaranteed by other Federal agencies totaled $30.9 billion on February 29, 2004, posting a decrease of $407.2 million from the level on January 31, 2004. This net change was the result of a decrease in holdings of agency debt (U.S. Postal Service) of $470.9 million and an increase in net holdings of government-guaranteed loans of $63.7 million. The FFB made 71 disbursements and received 6 prepayments during the month of February.

Below are tables presenting FFB February loan activity and FFB holdings as of February 29, 2004.

FEDERAL FINANCING BANK
February 2004 ACTIVITY

Borrower	*Date*	*Amount of*	*Final Maturity*	*Interest Rate*	*Annually or*

JS 1194

		Advance			*Semi-Annually*
AGENCY DEBT					
U.S. POSTAL SERVICE					
U.S. Postal Service	2/05	$900,000,000.00	2/6/2004	1.051%	Semi-Annually
U.S. Postal Service	2/05	$139,200,000.00	2/6/2004	1.010%	Semi-Annually
U.S. Postal Service	2/06	$800,000,000.00	2/9/2004	1.030%	Semi-Annually
U.S. Postal Service	2/06	$8,100,000.00	2/9/2004	1.010%	Semi-Annually
U.S. Postal Service	2/09	$600,000,000.00	2/10/2004	1.010%	Semi-Annually
U.S. Postal Service	2/10	$312,200,000.00	2/11/2004	1.030%	Semi-Annually
U.S. Postal Service	2/11	$149,700,000.00	2/12/2004	1.010%	Semi-Annually
U.S. Postal Service	2/13	$1,000,000,000.00	2/17/2004	1.010%	Semi-Annually
U.S. Postal Service	2/13	$69,300,000.00	2/17/2004	1.020%	Semi-Annually
U.S. Postal Service	2/17	$1,100,000,000.00	2/23/2004	1.020%	Semi-Annually
U.S. Postal Service	2/17	$471,600,000.00	2/19/1904	1.020%	Semi-Annually
U.S. Postal Service	2/16	$189,300,000.00	2/19/1904	1.051%	Semi-Annually
U.S. Postal Service	2/19	$22,100,000.00	2/20/2004	1.051%	Semi-Annually
U.S. Postal Service	2/23	$850,000,000.00	2/24/2004	1.051%	Semi-Annually
U.S. Postal Service	2/23	$8l,000,000.00	2/24/2004	1.071%	Semi-Annually
U.S. Postal Service	2/24	$650,000,000.00	2/25/2004	1.051%	Semi-Annually
U.S. Postal Service	2/24	$39,700,000.00	2/25/2004	1.092%	Semi-Annually
U.S. Postal Service	2/25	$400,000,000.00	2/26/2004	1.071%	Semi-Annually
U.S. Postal Service	2/25	$120,000,000.00	2/26/2004	1.081%	Semi-Annually
U.S. Postal Service	2/26	$304,900,000.00	2/27/2004	1.092%	Semi-Annually
U.S. Postal Service	2/27	$2,000,000,000.00	3/1/2004	1.081%	Semi-Annually
U.S. Postal Service	2/27	$61,400,000.00	3/1/2004	1.071%	Semi-Annually
GOVT-GUARANTEED LOANS					

GENERAL SERVICES ADMINISTRATION					
San Francisco OB	2/05	$132,507.93	8/1/2005	1.658%	Semi-Annually
San Francisco Bldg Lease	2/11	$18,463.06	8/1/2005	1.664%	Semi-Annually
San Francisco OB	2/23	$74,852.77	8/1/2005	1.607%	Semi-Annually
San Francisco OB	2/26	$132,507.94	8/1/2005	1.538%	Semi-Annually
San Francisco OB	2/26	$106;001.33	8/1/2005	1.538%	Semi-Annually
DEPARTMENT OF EDUCATION					
Virginia Union Univ.	2/04	$158,695.23	1/2/2032	4.772%	Semi-Annually
Livingstone College	2/23	$105,305.68	7/1/2031	4.732%	Semi-Annually
Livingstone College	2/23	$10,653.96	7/1/2031	4.732%	Semi-Annually
Livingstone College	2/23	$14,847.33	7/1/2031	4.732%	Semi-Annually
Tuskegee Univ.	2/26	$8,792,842.20	11/2/2026	4.496%	Semi-Annually
Tuskegee Univ.	2/26	$2,000,000.00	11/1/2004	1.096%	Semi-Annually
RURAL UTILITIES SERVICE					
Deep East Texas Electric #872	2/02	$6,440,000.00	12/31/2036	4.856%	Quarterly
Washington Electric #655	2/02	$425,000.00	1/2/2035	4.823%	Quarterly
Brown County Elec. #687	2/03	$450,000.00	6/30/2004	0.992%	Quarterly
Douglas Electric #725	2/03	$80,000.00	12/31/2035	4.859%	Quarterly
McLeod Coop. Power #554	2/03	$1,000,000.00	6/30/2004	0.992%	Quarterly
South Slope Cooperative #741	2/03	$1,763,000.00	1/2/2018	3.972%	Quarterly
East Kentucky Power #753	2/05	$6,500,000.00	12/31/2030	4.729%	Quarterly
McLennan County Elec. #784	2/05	$2,500,000.00	12/31/2035	4.685%	Quarterly
New Horizon Elec. #791	2/05	$1,500,000.00	6/30/2004	0.972%	Quarterly
North Star Elec. #2098	2/05	$1,500,000.00	12/31/2037	4.870%	Quarterly
Three River Electric Coop #846	2/05	$1,500,000.00	12/31/2036	4.852%	Quarterly
Delaware County Elec. #682	2/06	$750,000.00	1/2/2035	4.845%	Quarterly
San Patricio Elec. #676	2/06	$944,000.00	1/2/2035	4.845%	Quarterly

Vernon Electric Coop. #2008	2/06	$1,527,000.00	12/31/2036	4.878%	Quarterly
BARC Electric #663	2/09	$525,000.00	1/2/2035	4.777%	Quarterly
Blue Ridge Elec. #659	2/09	$8,850,000.00	12/31/2029	4.657%	Quarterly
TRANSCO #883	2/09	$6,343,000.00	12/31/2020	4.348%	Quarterly
Aiken Elec. #896	2/11	$3,698,000.00	12/31/2036	4.824%	Quarterly
Flint Elec. #2016	2/11	$2,956,000.00	3/31/2034	4.776%	Quarterly
West Florida Electric #2047	2/11	$4,397,000.00	12/31/2037	4.841%	Quarterly
Carroll Elec. #618	2/12	$400,000.00	1/3/2034	4.711%	Quarterly
French Broad Elec. #809	2/13	$3,000,000.00	12/31/2035	4.792%	Quarterly
Central Iowa Power Coop. #2092	2/17	$11,000,000.00	12/31/2013	3.371%	Quarterly
Central Iowa Power Coop. #2094	2/17	$3,000,000.00	12/31/2031	4.541%	Quarterly
East River Power #793	2/17	$4,619,000.00	6/30/2004	0.941%	Quarterly
Farmer's Rural Elec. #2046	2/17	$1,000,000.00	6/30/2004	0.941%	Quarterly
Swan's Island Electric #2037	2/17	$54,000.00	12/31/2036	4.782%	Quarterly
Forked Deer Electric #2069	2/19	$3,896,000.00	12/31/2037	4.793%	Quarterly
Upsala Coop. Te1e. #429	2/19	$82,590.00	6/30/2004	1.082%	Quarterly
West River Elec. #751	2/19	$4,000,000.00	6/30/2011	3.528%	Quarterly
Bartlett Elec. #535	2/20	$400,000.00	1/3/2034	4.782%	Quarterly
Dunn Electric Coop. #861	2/20	$500,000.00	12/31/2036	4.764%	Quarterly
Sac Osage Electric Coop. #815	2/20	$600,000.00	12/31/2036	4.764%	Quarterly
United Elec. #858	2/20	$1,045,000.00	12/31/2036	4.764%	Quarterly
Ravalli #641	2/24	$900,000.00	12/31/2029	4.614%	Quarterly
Red River Valley Elec. #2095	2/26	$3,000,000.00	6/30/2004	0.974%	Quarterly
Sangre De Cristo Elec. #732	2/26	$500,000.00	3/31/2011	3.448%	Quarterly
Piedmont Tel. #566	2/27	$217,739.00	12/31/2018	3.928%	Quarterly

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FEDERAL FINANCING BANK HOLDINGS

February 2004
(in millions of dollars)

Program	*Feb. 29, 2004*	*Jan. 31, 2004*	*Monthly Net Change 2/1/04- 2/29/04*	*Fiscal Year Net Change 10/1/03- 2/29/04*
Agency Debt:				
U.S. Postal Service	$20,061.4	$2,532.3	($470.9)	($5.2)
Subtotal*	$2,061.4	$2,532.3	($470.9)	($5,212.0)
Agency Assets:				
FmHA-RDIF	$680.0	$680.0	$0.0	($125.0)
FmHA-RHIF	$1,830.0	$1,830.0	$0.0	$0.0
Rural Utilities Service-CBO	$4,270.2	$4.270.2	$0.0	$0.0
Subtotal*	$6,780.2	$6,780.2	$0.0	($125.0)
Govt-Guaranteed Lending:				
DOD-Foreign Military Sales	$1,589.1	$1,622.7	($33.7)	($99.4)
DoEd-HBCU+	$126.1	$115.0	$11.1	$46.8
)HUD-Community Dev. Block Grant	$1.0	$1.0	$0.0	($1.2)
)HUD-Public Housing Notes	$1,054.8	$1,054.8	$0.0	($78.5)
;eneral Services Administration+	$2,139.4	$2,143.6	($4.3)	($7.8)
'OI-Virgin Islands	$8.2	$8.2	$0.0	($1.4)
ON-Ship Lease Financing	$597.3	$597.3	$0.0	($10.2)
ural Utilities Service	$16,426.5	$16,334.6	$91.9	$808.2
3A-State/Local Devel. Cos.	$68.4	$69.8	($1.3)	($8.9)
)T-Section 511	$3.0	$3.0	$0.0	$0.0
Subtotal*	$22,013.8	$21,950.1	$63.7	$647.8
Grand total*	**$30,855.4**	**$31,262.6**	**($4,072.0)**	**($4,689.2)**

**figures may not total due to rounding; +does not include capitalized interest*

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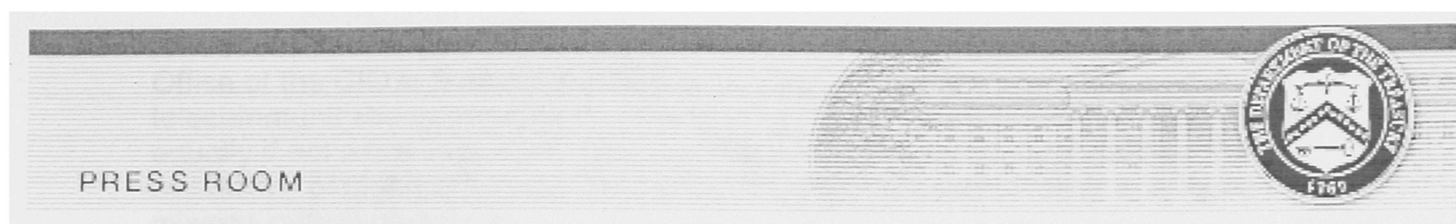
Last Updated on 3/25/04



FROM THE OFFICE OF PUBLIC AFFAIRS

February 26, 2004
js-1195

Testimony of
Drew Ladner, Chief Information Officer
United States Department of Treasury
Before the House Committee on Government Reform
February 26, 2004

Mr. Chairman and Members of the Committee, thank you for the opportunity to appear to discuss the General Services Administration's (GSA) government-wide telecommunications program, Networx. The Secretary of the Treasury welcomes this invitation for reasons relating to both the Department's mission and fiscal responsibility. The continued leadership of the Chairman and the Members of the Committee is vital if we are to steward taxpayer dollars wisely not only at the Treasury Department but across the federal government.

I serve as the Chief Information Officer (CIO) of the Treasury Department. As CIO I provide oversight, management, budgetary approval, and policy direction for all information technology programs within the Treasury Department and its bureaus. I have operational responsibility for shared services across all Treasury bureaus, including for the Treasury Communications System (TCS), one of the largest secure networks in the civilian government.

The Committee has requested the Treasury view on the Networx Request for Information. Let me start by suggesting a list of principles that the Treasury Department seeks to have inform its acquisition of telecommunications services. Reflected throughout my remarks below, they include but are not limited to:

1. Identifying and adopting innovation
2. Listening to the market laws of supply and demand
3. Relying on marketplace innovation
4. Avoiding the creation or promotion of proprietary standards
5. Simplifying business structures, processes, and systems
6. Embracing data, internet protocol, and managed services
7. Compensating based on performance and results
8. Affording maximum flexibility while keeping costs low
9. Supporting execution of Treasury shared service philosophy
10. Expecting technological obsolescence and not owning assets.

The Treasury Department seeks innovation in the acquisition of telecommunications services for two primary reasons. First, acquiring the most advanced telecommunications offerings provides the highest performance at the

lowest cost; because of the Department's large telecommunications program, the Office of the CIO is firmly committed to acquiring faster, cheaper, and better telecommunications services in order to exercise fiscal responsibility. Second, and equally if not more important, Treasury Department operations depend on the availability of high-performing telecommunications services in order to achieve mission-critical objectives.

The Treasury Department is committed to acquiring from the private sector the latest in telecommunications innovations, whether in product, process, or otherwise. New telecommunication services already have transformed traditional circuit-based voice communications into the digital world of IP-based communications. Because the private sector has the incentive to invest in research and development, the expectation is that the private sector consistently will provide the most attractive offerings in terms of cost and performance.

Today's question is: how does Networx fare in all of this? Early signs are that Networx will constitute a significant improvement over FTS 2001. It appears that Networx will be much more market-driven, in contrast to its more technology-driven predecessor, FTS 2001 (which was a follow on to FTS 2000). As a general rule, the government should rely on performance-based, results-oriented specifications rather than trying to dictate solutions through "how to" design technology specifications. Moreover, this underscores an essential philosophical approach to acquiring network services, whether the customer is in the public sector or private: government agencies should strive to ensure that the customer is provided with the most cost-effective service available.

Permit an illustrative example. Suppose a company has a need to transport products. There are two major options: (1) purchase parts from many suppliers, assemble trucks, use the trucks to transport products, and keep enough spare parts on hand to support a maintenance program; or (2) purchase fleet services from a trucking company. Option 1 will cost the company more and distract it from its core business. Option 2 reflects how telecommunications services should be acquired wherever possible, yielding the best price for performance.

Consequently, a properly configured Networx can provide a comprehensive set of management services that enables government agencies to acquire the telecommunications services required. A contract resembling FTS 2001 would be more circuit-centric, forcing agencies to fulfill the rest of its services by building and maintaining program management offices, unnecessarily decentralizing some telecommunications functions, and incurring more costs across the enterprise. For the Treasury Department, this would mean that each one of our dozen bureaus might have a relatively large telecommunications cost center. At the same time that administrative decisions are integrated enterprise-wide, it is important that other decision-making be as decentralized as possible.

This raises a larger point: as CIO I seek to manage the supply chain, both downstream from our shared service platform into Treasury bureaus as well as upstream into Treasury's suppliers. Treasury currently depends exclusively on no one carrier and manages risk by being carrier-neutral. Avoiding sole sourcing and preserving flexibility to use multiple companies across a large telecommunications contract are critical for several reasons. First, it is financially advantageous and ensures that competitive forces provide incentive for contractors to price at market levels. Second, in the event of technological change or obsolescence, a customer can make necessary adjustments quickly and cost-effectively. Third, if underperformance provides operational rationale to switch vendors, a government agency is in a better position to do so.

Managing the supply chain "upstream" is predicated on knowing what business problems require solutions and how to execute. Facilitating the implementation of new technologies is a crucial area where Networx can help federal agencies solve operational problems. For example, the Treasury Department is reviewing innovative solutions to improve billing processes and to reduce expenditures. With an FTS 2001-like contract it is difficult for an agency to initiate and to integrate the introduction, piloting, and deployment of new solutions and technologies. Key to a successful Networx contract will be to consolidate purchasing power in a flexible,

performance-based contract that nimbly accommodates innovation when superior price for performance can be achieved.

Shorter-term, performance-based contracts in which suppliers are driven by incentive make such an approach possible. Consequently, it allows the management of telecommunications relationships both at the business and technical levels. Because it is inadequate to have lengthy service level agreements (SLAs) that do not effectively address higher level business issues, the Treasury Department includes in its IT vision the integration of operating management into portfolio management. Telecommunications operations are no exception: customers or users with access to portfolio management tools can more clearly see and understand whether telecommunications services are meeting commitments and take managerial action as appropriate – also making the supply chain more efficient.

There is one final point on Networx that would boost IT security significantly: applying IT security solutions with equal rigor to backhaul networks. Traditional telecommunication carriers have increasing capabilities to monitor their core networks with intrusion detection, intrusion prevention, and other security technologies. While historically technical limitations have precluded fully using these security services to combat worms, spam, and other network vulnerabilities on high bandwidth, longer-haul portions of networks, innovation has made this possible in recent years. Networx should seek to ensure that its security services receive comparable treatment as large customers in the private sector. While diversified and localized monitoring is still required, integrated monitoring on a much larger scale can eliminate or reduce the risk of the most common vulnerabilities and prevent the further and wider spread of threats. The result of mandatory, centrally monitored, carrier-based intrusion detection system/intrusion prevention system would be bandwidth savings and a safer, more secure backbone for Networx and its customers.

Innovation is not just about our telecommunications programs; it is essential to national security. Economically, it enables us to do more with less. Politically, it promotes a leadership position on the global stage. Technologically, the application of new products and processes leads to even more advances – thanks to the vibrant entrepreneurial spirit of our country. And it is the lifeblood of the small- and medium-size businesses that drive 80 percent of our economy, the stability and prosperity of which is the mission of the Treasury Department.

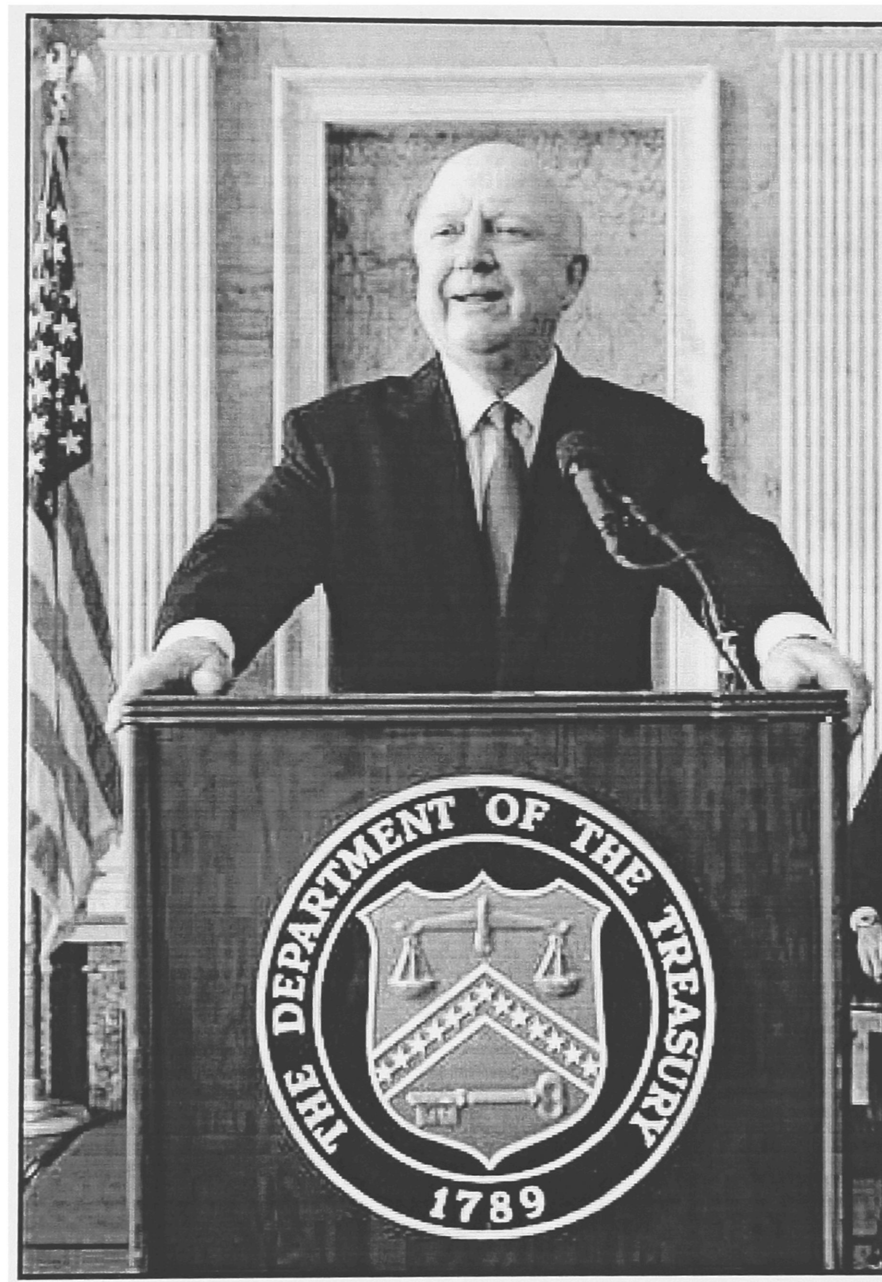
Again, I am grateful to the Committee for demonstrating leadership in exploring the best ways to acquire telecommunications services and for driving reform across the federal government. Mr. Chairman, thank you for the opportunity to appear before you today. This concludes my formal remarks, and I would be pleased to respond to any questions.

-30-

FROM THE OFFICE OF PUBLIC AFFAIRS

February 26, 2004
JS-1196

Photo: Deputy Secretary Samuel Bodman at the Treasury Department's Black History Month Celebration Event



Media Contact

Deputy Secretary Samuel Bodman spoke at the Treasury Department's Black History Month Celebration event. 2004 marks the 50th anniversary of the Supreme Court's landmark decision on Brown vs. Board of Education.

High Resolution Image

FROM THE OFFICE OF PUBLIC AFFAIRS

February 26, 2004
js-1197

U.S. Lifts Travel Ban on Libya

The United States today announced it will lift the travel ban on Libya. Today's action is a response to Libya's progress in joining the international community's efforts to combat terrorism and halt the spread of weapons of mass destruction and the missiles capable of delivering them.

The Libyan Sanctions Regulations were promulgated in January 1986 after Libya's participation in the terrorist attacks against the Rome and Vienna airports the month before. Authorized under the International Emergency Economic Powers Act and the International Security and Development Cooperation Act of 1985, the sanctions were a response to Libya's repeated use and support of terrorism against the United States, as well as other countries and innocent persons.

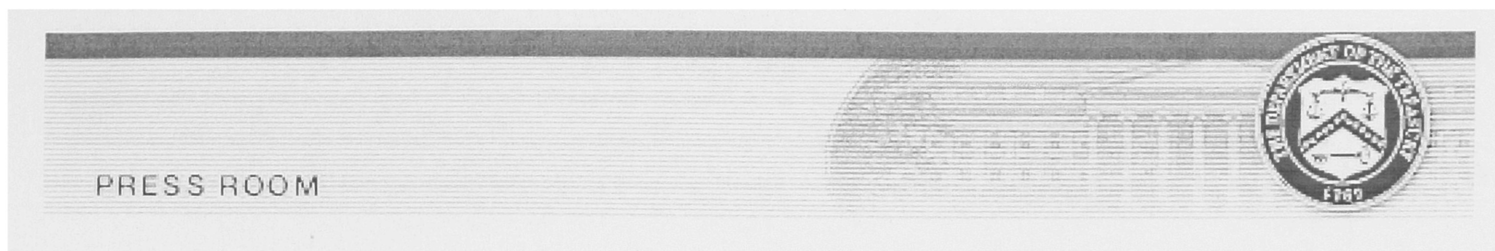
Among other things, the sanctions have prohibited U.S. citizens from engaging in travel and transportation-related activities with Libya. While the ban on travel by U.S. persons is being lifted today, the prohibitions on transportation-related activities, such as flights to Libya by U.S. air carriers, will remain in place at this time.

Lifting the travel ban will permit U.S. persons to engage in transactions related to travel to Libya and maintenance within Libya. Travel-related services, such as U.S. travel agents' booking of travel and accommodations within Libya for U.S. persons will also be permitted. Certain restrictions on payments, however, will continue to apply to these transactions.

The travel ban always exempted journalists regularly employed in such capacity by a newsgathering organization. U.S. citizens other than journalists were able to travel to Libya only under the following conditions:

- Travel by close family members of Libyan nationals when the U.S. citizen or resident registered with Treasury's Office of Foreign Assets Control or with the Embassy of Belgium in Tripoli;
- Travel for the sole purpose of engaging in licensed sales of agricultural commodities, medicine and medical devices; or
- Travel related to the installation or servicing of medical equipment exported pursuant to license could be authorized by specific license.

In addition, a limited number of specific licenses were issued for travel by U.S. companies with pre-sanctions holdings.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 26, 2004
JS-1198

MEDIA ADVISORY:Treasury to Hold Briefing on the 2003 Annual Financial Report of the United States Government

The Department of the Treasury will hold a briefing on Friday, February 27, 2004, to answer questions related to the 2003 Annual Financial Report of the United State Government.

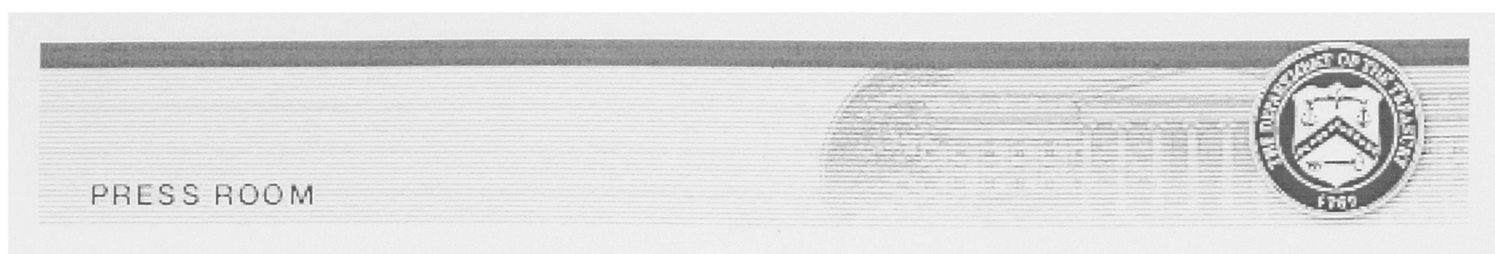
WHO: Don Hammond, Fiscal Assistant Secretary Robert Reid, Deputy Assistant Secretary for Accounting Operations

WHAT: Pen and Pad Briefing – no cameras will be admitted

WHEN: 2:00 pm EST

WHERE: Room **2224**

Media without Treasury press credentials planning to attend tomorrow's briefing should contact the Treasury Public Affairs office at 202/622-2960 by 9:30am, Friday morning. Media should be prepared to provide the following information: name, social security number and date of birth. Media with White House press credentials must call to be cleared in to the Treasury Building.



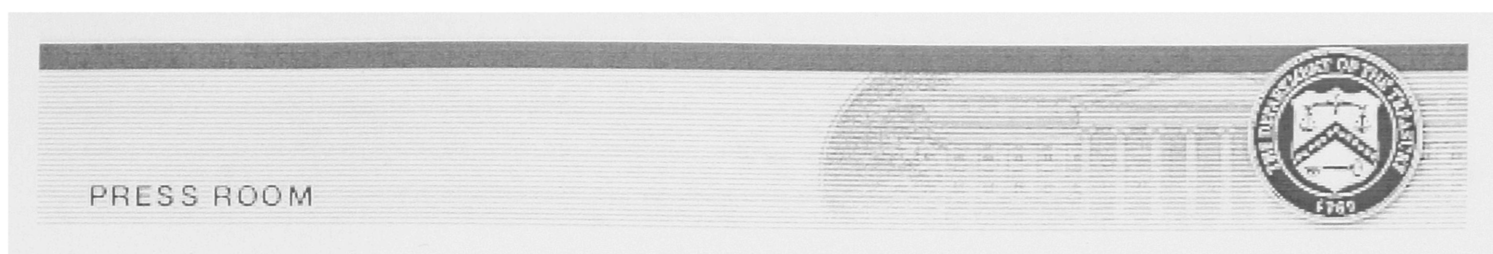
FROM THE OFFICE OF PUBLIC AFFAIRS

February 27, 2004
JS-1199

Statement of Acting Assistant Secretary for Economic Policy Mark Warshawsky on 2003 Fourth Quarter Gross Domestic Product Report

The economy continues to strengthen. A report this week on durable goods suggests continued rapid growth in business capital investment. This shows that the incentives contained in the President's Jobs and Growth plan are working.

Last year ended with a strong growth rate of 4.1 percent in the fourth quarter. The last half of 2003 saw the fastest rate of GDP growth in nearly 20 years and the economy looks to continue growing at levels above historical rates. We're encouraged by the continuing positive momentum we're seeing in the economy, but there remains more to be done. This Administration is committed to strengthening the environment for job creation and seeks to ensure that jobs are available for all those looking for work.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 26, 2004
JS-1200

Senior Treasury Department Official in Sacramento, CA, on Thursday Recognizes Local Financial Education Program

Treasury Assistant Secretary for Financial Institutions Wayne Abernathy today presented the Sacramento Mutual Housing Association, Sacramento, CA, with an honorary certificate of recognition for its efforts in teaching financial education to individuals in mutual housing communities throughout Sacramento, including non-English speaking residents.

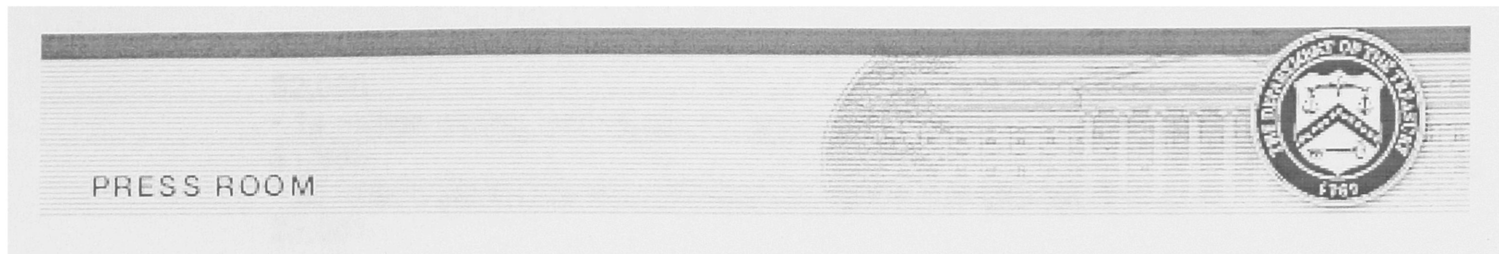
"This financial education program, which offers classes in languages such as Hmong, Russian, and Spanish, is an excellent example of how partnerships between community-based organizations, foundations, and financial institutions can make the financial mainstream more accessible to all people in the United States, whether they have lived here their entire lives or only recently arrived in this country," said Assistant Secretary Abernathy. "It is rewarding to hear how the graduates of this program have used what they have learned to go on to purchase a first home, pursue higher education, or start a small business."

The Financial Education Workshop Series began in the spring of 2001 and is free to all participants. "At Sacramento Mutual Housing Association we believe that financial education and individual development accounts are crucial components to building assets for low-income families and communities," said Rachel Iskow, Executive Director. "We are honored that Secretary Abernathy is recognizing the innovativeness of this program and the hardworking families that are using these tools to break free from poverty."

The Sacramento Mutual Housing Association is a non-profit corporation that develops, owns, and operates affordable multi-family housing to serve the community interest. Its mission is to develop and operate permanently affordable housing that builds strong and stable communities through resident participation and leadership development. The Financial Education Workshop Series is a collaborative effort of the Sacramento Mutual Housing Association, Mercy Housing California, and the Sacramento Valley Organizing Community, supported by the American Express Foundation, the Allstate Foundation, and the Neighborhood Reinvestment Corporation. The Workshop consists of six two-hour classes covering topics such as budgeting, basic banking, credit improvement and maintenance, money management, being a smart consumer, and building assets.

The Treasury Department's Office of Financial Education has been designated by Congress to lend its expertise and provide primary support to the Commission to assist it in fulfilling its functions and duties. The Office of Financial Education (OFE) was established in May 2002, as part of the Treasury Department's long-term commitment to ensure that all Americans have access to financial education programs that will help them make informed financial decisions throughout their lives.

More information about the OFE can be found at:
www.treasury.gov/financialeducation



FROM THE OFFICE OF PUBLIC AFFAIRS

February 19, 2004
JS-1201

Treasury Releases New Data On The Benefits Of The Jobs And Growth Tax Relief Reconciliation Act

(Revised)

The Department of the Treasury today released new figures demonstrating that because of the President's tax relief package enacted last May, an additional $50 billion dollars will remain in the hands of American taxpayers through higher refunds and lower tax payments this spring. The total refunds Americans will receive this spring will increase to about $195 billion.

• As a result of the tax cuts in 2003, Treasury expects that a record number of individuals will receive refunds this year.
• Treasury expects that the average refund will be $300 higher than had the Jobs & Growth Tax Relief Act had not been enacted.
• The President's 2003 tax relief is expected to increase refunds received by Americans by about $37 billion more than if the Jobs & Growth Tax Relief Act had not been enacted, from approximately $158 billion to $195 billion.
• The tax relief is expected to decrease the amount that Americans who must make tax payments when filing their tax returns this spring by approximately $13 billion, from $85 billion to $72.5 billion.
• Taken together the higher tax refunds and lower tax payments are expected to put an additional $50 billion in the hands of American taxpayers this spring.

In addition, Treasury's data shows that American families will see a significant reduction in their tax burden because of the tax relief packages that the President has signed since taking office. The President's 2001 and 2003 tax cuts mean that in 2004:

• Americans will receive a total of $232 billion in tax relief in 2004.
• $176 billion in tax relief will stay in the hands of American families and small businesses to help then save and invest.
• Every American who would have paid income taxes before the tax relief was enacted in 2001 will receive a tax cut in 2004.

The President's Tax Cuts Mean Significant Tax Relief for Working American Families Expanding the 10% bracket and doubling the child tax credit will benefit low income Americans

• Nearly 5 million taxpayers, including 4 million taxpayers with children, will have their income tax liability completely eliminated in 2004.
• Low-income families will also benefit from provisions that make the child credit refundable for more families and reduce marriage penalties caused by the EITC. 111 million individuals and families will receive an average tax cut of $1,586 in 2004 because of the tax cutes of 2001 and 2003.

• 49 million married couples will have an average tax cut of $2,602.

• 43 million families with children will receive an average tax cut of $2,090.
• 14 million elderly individuals will see their taxes fall, on average, by $1,883.
• 25 million small business owners will receive an average tax cut of $3,001.

If Congress Does Not Act, Americans Will Pay Higher Taxes in 2005

If the tax cuts that expire after 2004 are not extended for 2005, taxes will increase for taxpayers who otherwise would benefit from these provisions.

• Lower income taxpayers will not receive $5.7 billion in relief from the expanded 10 percent rate.
• Taxpayers will not receive $8.9 billion in marriage penalty tax relief
• Families with children will not receive $13.2 billion in relief from the child tax credit. In 2005, the increased child credit, additional marriage penalty relief, and expanded 10 percent bracket will sunset, increasing the tax burden on a family of four earning $40,000 by $915.

93 million taxpayers would pay, on average, a tax increase of $565.

• 70 million women would see their taxes increase, on average, by $697
• 46 million married couples would pay, on average, an additional $960 in taxes
• 37 million families with children would incur an average tax increase of $954
• 8 million single women with children would see their taxes increase, on average, by $357
• 11 million elderly taxpayers would pay, on average, an additional $398 in taxes
• 23 million small business owners would incur tax increases averaging $831
• Nearly 2 million individuals and families who currently have no income tax liability would become subject to the income tax.
• President Bush's budget extends AMT relief through 2005. Without these changes, these taxpayers would pay an additional $23.2 billion in tax as a result of the AMT.

PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 27, 2004
JS-1202

**U.S. Treasury Secretary John Snow Center for Strategic and International Studies
Washington, DC February 27, 2004**

Good afternoon. I am very pleased to join this esteemed group and to talk with you about the outlook for the global economy.

The global economic recovery has accelerated in the last six months. Economic stability is also improving, and risks have diminished. Consensus forecasts put G-7 growth at 3.3% for this year, more than double the 2002 rate.

In the United States, the recovery is strengthening. The President's tax cuts have worked. They provided the stimulus that was necessary to turn the economy around, and they are now encouraging and allowing for the economic growth that is continuing into the future.

- Economic growth in the second half of 2003 was the fastest since 1984;
- New home construction in 2003 was the highest in 25 years;
- Homeownership levels are at historic highs;
- Manufacturing activity is increasing;
- Inflation and interest rates are low;
- Jobs are coming back;
- The unemployment rate is falling;
- There is more than three trillion dollars of growth in value in the markets last year.

These economic indicators all point to the same conclusion: We are on a path to sustained economic growth. However, there is more to do. We are not, by any means, satisfied. We will keep working until every American who wants work can find a job.

Beyond the United States, we are also seeing promising signs. Japanese performance provided a positive surprise in the fourth quarter, with growth hitting an annual rate of 7 percent. Recent Japanese recoveries, including this one, have been heavily dependent on export demand. It is important for domestic demand to play a greater role to bring about sustained growth in the Japanese economy.

In continental Europe, where growth is still lagging, the indicators are positive. German growth finally turned around in the second half of last year. Industrial production was up sharply in the fourth quarter of 2003, and business surveys look good. Nonetheless, overall growth in the Euro Area remained modest last year, especially in the biggest countries. It is important that the positive signs become growth achievements this year.

Many emerging market countries are also experiencing higher economic growth rates, along with reduced interest rate spreads and improved equity markets. This follows concerted efforts to reform the international financial system through steps such as inclusion of collective action clauses in emerging market debt, limits on exceptional access to IMF lending, measuring and accounting for results, and the use of grants to avoid heavy debt burdens.

Looking ahead, prospects also look positive. There is evidence that the momentum for growth continues to build. Financial markets have strengthened – in the U.S. and elsewhere. Inventories are low – suggesting the need to increase production to meet demand. And more investment is underway. More broadly, there is a more positive outlook, as geopolitical uncertainties have eased and forecasters see fewer downside risks.

Yet this is not enough. Stronger growth is in everyone's interest. More work is needed to ensure growth that is broad-based and sustainable – and less reliant on a single engine. It is not in anyone's interest that the United States consistently stand out as the fastest growing major economy.

Indeed, the need for stronger global growth was at the top of the agenda when I hosted my G-7 colleagues in Boca Raton earlier this month. We all place top priority on growth. And we agreed that structural reforms are vital to our long-term performance – even if they involve short term costs.

This is why I felt it was so important to move ahead with what we are calling the Agenda for Growth initiative, which was launched by the G-7 last September. This initiative focuses on supply-side reforms to boost productivity, raise growth and employment, and thereby increase living standards. In other words, while strong macroeconomic policies are vital, it is also essential that we update microeconomic frameworks in the major economies to enhance the potential for sustained and healthy growth.

We are now seeing progress as each G-7 country is taking concrete actions to advance these goals. For example:

- Canada has fully implemented a five-year, $100 billion tax reduction plan.
- France is undertaking pension reforms that will significantly strengthen its public finances.
- Germany has enacted key elements of its reform initiative – entitled Agenda 2010 – that includes measures to improve work incentives as well as to reduce taxes.
- Italy has seen its unemployment rate fall as labor market reforms entered fully into force in October.
- The United Kingdom announced new measures to help small business access capital and to improve access to tax credits for research and design.

In Boca Raton, we all committed to future steps that demonstrate the widespread commitment to going further to increase labor and product market flexibility, boost productivity and raise employment.

- The United Kingdom is establishing a long-term strategy for funding innovation and scientific research, extending skills training programs and is proposing a collaborative initiative on regulatory reform across the EU.
- Japan will work on further fiscal expenditure and revenue reforms, including in social security, and will continue to address financial sector reforms.
- Italy plans to advance pension and corporate tax reform, including tax exemptions on dividends and capital gains.
- Germany's priorities include pension and tax code reform.
- France will continue its work to reduce labor market constraints, while also pursuing health care reform.
- Canada will provide tax incentives and explore other funding alternatives for infrastructure investment by municipalities.

As for the United States, our contributions will be through the President's commitments to maximize growth and job creation. This includes: spurring saving through changes to the tax system; making health care more affordable; working to prevent frivolous lawsuits from diverting money from job creation; streamlining regulations; preparing American workers for the demands of the 21st century job market; and working to make tax relief permanent, so that families and businesses alike can plan for the future.

The Agenda for Growth marks a fundamental change in the G-7 approach. I am optimistic that the steps that each country is pursuing will make a real difference to our future prospects and those of the world economy as a whole. Combined with strong macroeconomic policies, including sound fiscal policies over the medium-term, this initiative is also an important step to addressing global current account imbalances.

Let me turn to trade. Opening markets and reducing barriers to trade is an important engine for domestic and global economic growth; trade leads to more jobs, higher wages and increased productivity, which in turn leads to greater prosperity. It is through free trade that all nations can benefit from each other's prosperity. Free trade means new markets for exporters.

Multilateral trade liberalization is a global tax cut for all consumers and exporters and an engine for growth, in association with sound macroeconomic and structural policies. The IMF and World Bank estimate that the static global welfare gains from eliminating barriers to merchandise trade alone are broadly in the range of $250 billion to $550 billion per year. Another study estimates the gains from removing all trade barriers at $1.9 trillion.

The Cancun outcome represented a missed opportunity, but there are hopeful signs that we can get the Doha Development Agenda back on track again so that 2004 is not a lost year. The focus of the WTO negotiations should be the market access agenda – agriculture, industrial and consumer goods, and services. These areas have the greatest potential to promote economic growth. For developing countries to realize the benefits of trade, they too need to reduce their own trade barriers substantially. Developing countries collect most of their tariffs on trade with other developing countries. In particular, efficiency gains from trade liberalization in the financial services sector could be beneficial for many emerging markets.

But even as we ponder the next steps in the WTO, the United States continues to press an aggressive trade agenda to open markets regionally and bilaterally with willing partners. For example, we have recently concluded free trade agreements with Central America (CAFTA) and Australia, and are negotiating additional free trade agreements in Africa, Asia, Latin America, and the Middle East. By moving forward on multiple fronts, we can exert leverage for openness and create a new competition for trade liberalization.

Before closing, I want to mention briefly some of the other important initiatives we are pursuing as part of the drive for global growth. With the chairmanship of the G-7 this year, we have the opportunity to help lead change and bring results that facilitate growth.

In Boca Raton, we focused in particular on:

- Supporting the economic revival underway in Afghanistan and Iraq – as well as the importance of strengthening economic growth and raising living standards in the greater Middle East.
- Continuing the fight against terrorist financing – notably strengthening asset freezing regimes and combating abuse of the informal financial sector and non-profit organizations.
- Creating an environment that allows private businesses to flourish in the poorest countries.
- Reducing the roadblocks for people sending money back to their families – by identifying and removing the barriers that slow the flow of remittances, make transactions expensive or encourage money to flow through informal channels.

Looking to the Summit, I expect us to continue our work in these areas, as well as to explore ways to consolidate and build on reforms to the international financial system so that it is as modern and effective as possible.

Thank you so much for having me here today – I hope you have a wonderful meeting.

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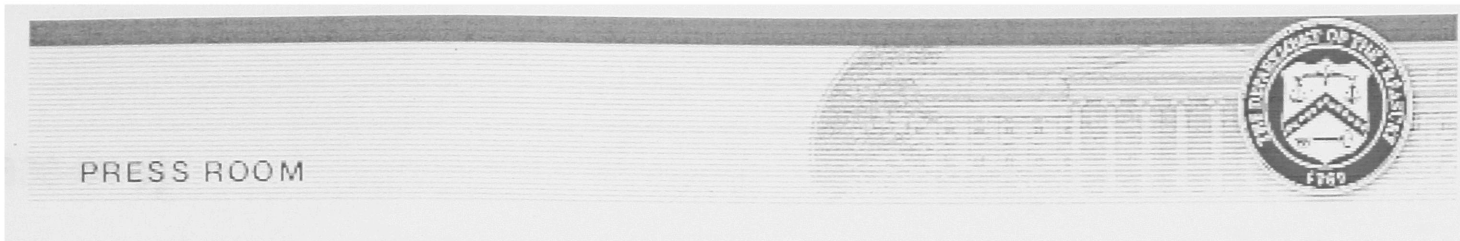

FROM THE OFFICE OF PUBLIC AFFAIRS

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February 27, 2004
JS-1203

Treasury and IRS Issue Depreciation Regulations

Today, the Treasury Department and Internal Revenue Service issued proposed and temporary regulations that provide guidance for computing depreciation deductions under the Modified Accelerated Cost Recovery System (MACRS) in section 168 of the Internal Revenue Code when property is acquired in a like-kind exchange or as a result of an involuntary conversion.

"Previously, the depreciation rules for MACRS property acquired in a like-kind exchange or involuntary conversion transaction were unclear. These regulations provide clear rules to taxpayers depreciating property acquired and relinquished in these transactions," stated Acting Treasury Assistant Secretary for Tax Policy Greg Jenner.

The regulations also provide guidance on the annual depreciation allowances for automobiles that are both acquired in a like-kind exchange or involuntary conversion transaction and subject to the special automobile depreciation limitations in section 280F.

The regulations generally apply to like-kind exchange and involuntary conversion transactions after February 27, 2004. Taxpayers generally may rely on these regulations, or any prior guidance issued by the Internal Revenue Service, for MACRS property acquired in a like-kind exchange or involuntary conversion transaction before the effective date of the regulations.

Related Documents:

- TD 9115: Final and temporary regulations
- REG-106590-00: Notice of proposed rulemaking

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9115]

RIN 1545-BC27

Depreciation of MACRS Property That is Acquired in a Like-kind Exchange or As a Result of an Involuntary Conversion

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains regulations relating to the depreciation of property subject to section 168 of the Internal Revenue Code (MACRS property). Specifically, these temporary regulations provide guidance on how to depreciate MACRS property acquired in a like-kind exchange under section 1031 or as a result of an involuntary conversion under section 1033 when both the acquired and relinquished property are subject to MACRS in the hands of the acquiring taxpayer. These temporary regulations will affect taxpayers involved in a like-kind exchange under section 1031 or an involuntary conversion under section 1033. The text of these temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section in this issue of the **Federal Register**.

DATES: Effective Dates: These regulations are effective March 1, 2004.

111 pp.

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-106590-00, REG-138499-02]

RIN 1545-AX95; RIN 1545-BB05

Depreciation of MACRS Property That is Acquired in a Like-kind Exchange or As a Result of an Involuntary Conversion

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking; notice of proposed rule making by cross-reference to temporary regulations; notice of public hearing; and partial withdrawal of proposed regulations.

SUMMARY: In the Rules and Regulations section of this issue of the **Federal Register**, the IRS is issuing temporary regulations relating to the depreciation of property subject to section 168 of the Internal Revenue Code (MACRS property). Specifically, the temporary regulations provide guidance on how to depreciate MACRS property acquired in a like-kind exchange under section 1031 or as a result of an involuntary conversion under section 1033 when both the acquired and relinquished property are subject to MACRS in the hands of the acquiring taxpayer. The text of those temporary regulations also serves as the text of these proposed regulations. This document also provides notice of a public hearing on these proposed regulations and a partial withdrawal of proposed regulations [REG-139499-02] published July 21, 2003.

DATES: Written or electronic comments must be received by May 30, 2004. Outlines

of topics to be discussed at the public hearing scheduled for June 3, 2004, at 10 a.m. must be received by May 13, 2004.

ADDRESSES: Send submissions to CC:PA:LPD:PR (REG-106590-00), room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Alternatively, submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-106590-00), Courier's Desk, Internal Revenue Service, 1111 Constitution Ave., NW, Washington, DC, or sent electronically, via the IRS Internet site at http://www.irs.gov/regs. The public hearing will be held in the Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Charles J. Magee, (202) 622-3110; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Robin Jones, (202) 622- 7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

Temporary regulations in the Rules and Regulations section of this issue of the **Federal Register** amend 26 CFR part 1 relating to section 168 of the Internal Revenue Code (Code). The temporary regulations provide guidance under section 168 on how to depreciate MACRS property acquired in a like-kind exchange under section 1031 or as a result of an involuntary conversion under section 1033 when both the acquired and relinquished property are subject to MACRS in the hands of the acquiring taxpayer.

The text of those regulations also serves as the text of these proposed

regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they may be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for June 3, 2004, beginning at 10 a.m. in the Auditorium of the Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must enter at the

Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the **FOR FURTHER INFORMATION CONTACT** section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by May 13, 2004. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal authors of these regulations are Alan H. Cooper, Office of the Chief Counsel (Small Business/Self Employed), and Charles J. Magee, Office of the Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Partial Withdrawal of Proposed Regulations

Under the authority of 26 U.S.C. 7805, §§1.168(a)-1 and 1.168(b)-1 of the notice of proposed rulemaking (REG-138499-02) published in the **Federal Register** on July 21, 2003, (68 FR 43047) are withdrawn.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1–INCOME TAXES

Paragraph 1. The authority citation for part 1 reads as follows:

Authority: 26 U.S.C. 7805 * * *

§1.168(i)-1 also issued under 26 U.S.C. 168(i)(4).

Par. 2. Sections 1.168(a)-1 and 1.168(b)-1 are added to read as follows:

§1.168(a)-1 Modified accelerated cost recovery system.

[The text of this proposed section is the same as the text of §1.168(a)-1T(a) and (b) published elsewhere in this issue of the **Federal Register**].

§1.168(b)-1 Definitions.

[The text of this proposed section is the same as the text of §1.168(b)-1T(a) and (b)(1) published elsewhere in this issue of the **Federal Register**].

Par. 3. Section 1.168(d)-1 is amended to read as follows:

1. Revising paragraph (b)(3)(i) and (ii).

2. Adding paragraph (d)(3).

The revision and addition read as follows:

§1.168(d)-1 Applicable conventions—half-year and mid-quarter conventions.

* * * * *

(b) * * *

(3) * * *

(i) and (ii) [The text of the proposed amendment to §1.168(d)-1(b)(3)(i) and (ii) is the same as the text of §1.168(d)-1T(b)(3)(i) and (ii) published elsewhere in this issue of the **Federal Register**].

* * * * *

(d) * * *

(3) [The text of the proposed amendment to §1.168(d)-1(d)(3) is the same as the text of §1.168(d)-1T(d)(3) published elsewhere in this issue of the **Federal Register**.]

Par. 4. Section 1.168(i)-0 is amended by revising the entries for §1.168(i)-1(d)(2), (e)(3)(i), (e)(3)(v) and (vi), (f)(1), (f)(2), (f)(2)(i), (i), (j), and (l) to read as follows:

' 1.168(i)-0 Table of contents for the general asset account rules.

* * * * *

§1.168(i)-1 General asset accounts.

* * * * *

(d) * * *

(2) [The text of the proposed entry for §1.168(i)-1(d)(2) is the same as the entry for §1.168(i)-1T(d)(2) published elsewhere in this issue of the **Federal Register**].

* * * * *

(e) * * *

(3) * * *

(i) [The text of the proposed entry for §1.168(i)-1(e)(3)(i) is the same as the entry for §1.168(i)-1T(e)(3)(i) published elsewhere in this issue of the **Federal Register**].

* * * * *

(vi) [The text of the proposed entries for §1.168(i)-1(e)(3)(vi) is the same as the entries for §1.168(i)-1T(e)(3)(vi) published elsewhere in this issue of the **Federal Register**].

* * * * *

(f) * * *

(f)(1) through (f)(2)(i) [The text of the proposed entries for §1.168(i)-1(f)(1) through (f)(2)(i) is the same as the text of the entries for §1.168(i)-1T(f)(1) through (f)(2)(i) published elsewhere in this issue of the **Federal Register**].

* * * * *

(i) and (j) [The text of the proposed entries for §1.168(i)-1(i) and (j) is the same as the entries for §1.168(i)-1T(i) and (j) published elsewhere in this issue of the **Federal Register**].

* * * * *

(l) [The text of the proposed entry for §1.168(i)-1(l) is the same as the entry for §1.168(i)-1T(l) published elsewhere in this issue of the **Federal Register**].

Par. 5. Section 1.168(i)-1 is amended by revising paragraphs (c)(2)(ii)(E), (d)(2), (e)(3)(i), (e)(3)(iii)(B)(4), (e)(3)(vi), (f)(1), (f)(2)(i), (i), (j), and (l) to read as follows:

§1.168(i)-1 General asset accounts.

* * * * *

(c) * * *

(2) * * *

(ii) * * *

(E) [The text of the proposed amendment to §1.168(i)-1(c)(2)(ii)(E) is the same as the text of §1.168(i)-1T(c)(2)(ii)(E) published elsewhere in this issue of the **Federal Register**].

* * * * *

(d) * * *

(2) [The text of the proposed amendment to §1.168(i)-1(d)(2) is the same as the text of §1.168(i)-1T(d)(2) published elsewhere in this issue of the **Federal Register**].

* * * * *

(e) * * *

(3) * * *

(i) [The text of the proposed amendment to §1.168(i)-1(e)(3)(i) is the same as the text of §1.168(i)-1T(e)(3)(i) published elsewhere in this issue of the **Federal Register**].

* * * * *

(iii) * * *

(B) * * *

(4) [The text of the proposed amendment to §1.168(i)-1(e)(3)(iii)(B)(4) is the same as the text of §1.168(i)-1T(e)(3)(iii)(B)(4) published elsewhere in this issue of the **Federal Register**].

* * * * *

(e)(3)(vi) [The text of the proposed amendment to §1.168(i)-1(e)(3)(vi) is the same as the text of §1.168(i)-1T(e)(3)(vi) published elsewhere in this issue of the **Federal Register**].

* * * * *

(f)(1) and (2) [The text of the proposed amendment to §1.168(i)-1(f)(1) and (2) is the same as the text of §1.168(i)-1T(f)(1) and (2) published elsewhere in this issue of the **Federal Register**].

* * * * *

(i) and (j) [The text of the proposed amendment to §1.168(i)-1(i) and (j) is the same as the text of §1.168(i)-1T(i) and (j) published elsewhere in this issue of the **Federal Register**].

* * * * *

(l) [The text of the proposed amendment to §1.168(i)-1(l) is the same as the text of §1.168(i)-1T(l)(1) through (l)(3)(i) published elsewhere in this issue of the **Federal Register**].

Par. 6. Section 1.168(i)-5 is added to read as follows:

§1.168(i)-5 Table of contents.

[The text of this proposed section is the same as the text of §1.168(i)-5T published elsewhere in this issue of the **Federal Register**].

Par. 7. Section 1.168(i)-6 is added to read as follows:

§1.168(i)-6 Like-kind exchanges and involuntary conversions.

[The text of this proposed section is the same as the text of §1.168(i)-6T published elsewhere in this issue of the **Federal Register**].

Par. 8. Section 1.168(k)-1 is added to read as follows:

§1.168(k)-1 Additional first year depreciation deduction.

(a) through (f)(5)(ii)(F)(1) [Reserved]. For further guidance, see §1.168(k)-1T(a) through (f)(5)(ii)(F)(1).

(2) [The text of the proposed amendment to §1.168(k)-1(f)(5)(ii)(F)(2) is the same as the text of §1.168(k)-1T(f)(5)(ii)(F)(2) published elsewhere in this issue of the **Federal Register**].

(f)(5)(ii)(G) through (f)(5)(iv) [Reserved]. For further guidance, see §1.168(k)-1T(f)(5)(ii)(G) through (f)(5)(iv).

(v) [The text of the proposed amendment to §1.168(k)-1(f)(5)(v) is the same as the text of §1.168(k)-1T(f)(5)(v) published elsewhere in this issue of the **Federal Register**].

(f)(6) through (f)(9) [Reserved]. For further guidance, see §1.168(k)-1T (f)(6) through (f)(9).

(g) Effective date. (1) [The text of the proposed amendment to §1.168(k)-1(g)(1) is the same as §1.168(g)-1T(g)(1)(i) published elsewhere in this issue of the **Federal Register**].

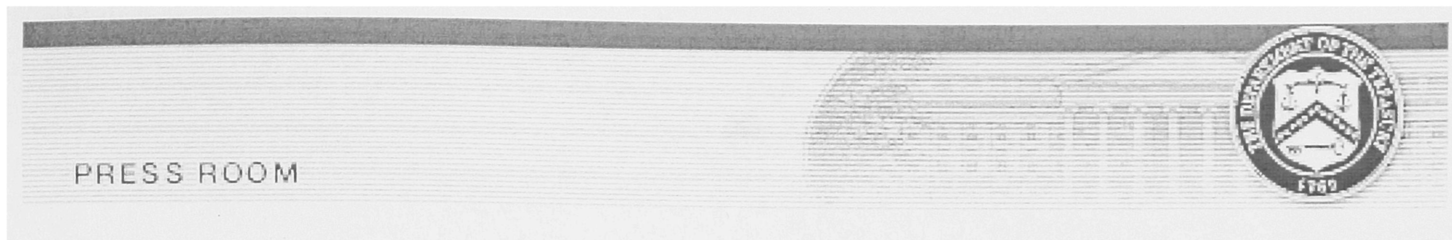
(2) [Reserved]. For further guidance, see §1.168(k)-1T(g)(2).

(3)(i) and (ii) [The text of the proposed amendment to §1.168(k)-1(g)(3)(i) and (ii) is the same as the text of §1.168(k)-1T(g)(3)(i) and (ii) published elsewhere in this issue of the **Federal Register**].

(g)(4) [Reserved]. For further guidance, see §1.168(k)-1T(g)(4).

/s/ Mark E. Matthews

Deputy Commissioner for Services and Enforcement.



FROM THE OFFICE OF PUBLIC AFFAIRS

February 27, 2004
JS-1204

U.S. Government Releases FY 2003 Financial Report

The Treasury Department and Office of Management and Budget today released the fiscal year 2003 Financial Report of the United States Government, a comprehensive look at the government's finances that complements the Budget of the U.S. Government. The report provides financial information for all aspects of the federal government.

"Just as we demand that public companies accurately report financial information to their shareholders, the federal government has an obligation to present its financial position in a complete and timely manner to America's taxpayers. We will continue to make improvements in reporting processes throughout the federal government to produce and report information that meets the highest standards," said Treasury Secretary Snow.

As part of our efforts to provide timely and accurate reporting, this year's Financial Report is being issued a month earlier than last year, a clear indication that the government is making progress in accelerating its reporting. For FY 2003, three-fourths of the major government agencies had completed their audited financial statements by the end of December. Even more important, eight agencies issued their statements by mid-November, only 45 days after the end of the fiscal year and one year ahead of 2004 reporting requirements. In addition, these eight agencies received unqualified opinions.

This year's report reflects information from the Department of Homeland Security with its transfer of 22 government agencies and offices and some 180,000 employees. The creation of the Department of Homeland Security in 2003 was the most significant transformation of the Federal Government since 1947 when the various branches of the Armed Forces were merged into a new Department of Defense.

An important reporting improvement this year was the adoption of a new accounting standard that requires recording military equipment and its related depreciation as an asset. The estimated total acquisition cost of this equipment was $1.2 trillion.

The 2003 financial results show an accrual-based net operating cost of $665 billion, compared to the reported budget deficit of $374.8 billion. The main difference between the two results is that the Financial Report includes post-employment actuarial costs for veterans' benefits and civilian and military retirees' pensions and health care. The government's largest liability for FY 2003 was debt held by the public, which was $3.9 trillion. The report's Management Discussion and Analysis section addresses the full effects of all significant liabilities, stewardship responsibilities, and other commitments.

While much progress had been made in the Federal Government's financial reporting this past year, some challenges remain. The General Accounting Office issued a disclaimer of opinion on the report and cited some material weaknesses in data and processes. We have been working to eliminate these problems; however, making these improvements will require a concerted effort by all government agencies and auditors, along with continued strong leadership from Treasury and OMB.

The full report can be found at http://www.fms.treas.gov/fr/

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PRESS ROOM

FROM THE OFFICE OF PUBLIC AFFAIRS

February 27, 2004
js-1205

FATF Strengthens Campaign to Fight Money Laundering and Terrorist Financing

At its Plenary meeting in Paris today, the Financial Action Task Force (FATF), the international body leading the charge to safeguard the global financial system against money laundering and terrorist financing, announced the removal of Egypt and Ukraine from its list of Non-Cooperative Countries and Territories (NCCTs).

"The international community, through the FATF, continues to remain vigilant and act against the threat of money laundering and terrorist financing. Today's announcement is a clear indication that we are making important progress in building the international net to prevent and catch the flow of tainted money through the financial system," said Juan Zarate, the U.S. Treasury Department's Deputy Assistant Secretary for the Executive Office of Terrorist Financing and Financial Crimes.

NCCTs are countries that have failed to adopt and implement adequate measures to effectively fight money laundering. Countries on the NCCT list can be subjected to a range of counter measures, including increased scrutiny when dealing with banks abroad.

Seven countries still remain on list: Cook Islands, Guatemala, Indonesia, Myanmar, Nauru, Nigeria and Philippines.

Also today, the FATF President expressed support for the continuation of the successful collaboration between FATF and the IMF and World Bank. The three institutions recently conducted a 12-month pilot program to ensure the consistent application of anti-money laundering and anti-terrorist financing standards worldwide. The IMF and World Bank used the FATF's 40 Recommendations on Money Laundering and Eight Special Recommendations Against Terrorist Financing to assess countries' financial systems during the program.

The FATF encouraged the IMF and World Bank to continue such assessments on a comprehensive, uniform and permanent basis as a regular part of their Financial Sector Assessment Program.

Before the start of the Plenary meeting earlier this week, the FATF held a seminar on the international fight against the financial war on terrorism. Attended by 44 countries, the seminar addressed the risks posed by alternative remittance systems, cash couriers, non-profit organizations and the links between narcotics trafficking and terrorist financing.

Attendees expressed the need for improved resources to better collect and share information regarding terrorist financing throughout the global economy. The FATF, a 31-member body, is committed to ensuring the implementation of practical steps to help the international community achieve this goal.

"This is an important dialogue as the international community adapts to the changing complexion of terrorist financing and the threat it poses to all of us," Zarate continued.

The seminar came after the Finance Ministers and Central Bank Governors of the G-7 and invited countries made a political commitment to combat terrorist financing during the September 2003 meeting in Dubai.

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