

1 **ADD SECTIONS 671 AND 672**  
2 **FROM SENATE-PASSED H. 4520**  
3 **WITH THE MODIFICATIONS AS**  
4 **FOLLOWS**

5 **SEC. 671. TREATMENT OF NONQUALIFIED DEFERRED COM-**  
6 **PENSATION PLANS.**

7 (a) IN GENERAL.—Subpart A of part I of subchapter  
8 D of chapter 1 is amended by adding at the end the fol-  
9 lowing new section:

10 **“SEC. 409A. INCLUSION IN GROSS INCOME OF DEFERRED**  
11 **COMPENSATION UNDER NONQUALIFIED DE-**  
12 **FERRED COMPENSATION PLANS.**

13 “(a) RULES RELATING TO CONSTRUCTIVE RE-  
14 CEIPT.—

15 “(1) IN GENERAL.—

16 “(A) GROSS INCOME INCLUSION.—If at  
17 any time during a taxable year a nonqualified  
18 deferred compensation plan—

19 “(i) fails to meet the requirements of  
20 paragraphs (2), (3), (4), and (5), or

21 “(ii) is not operated in accordance  
22 with such requirements,

23 all compensation deferred under the plan for  
24 the taxable year and all preceding taxable years  
25 shall be includible in gross income for the tax-

1           able year to the extent not subject to a substan-  
2           tial risk of forfeiture and not previously in-  
3           cluded in gross income.

4           “(B) INTEREST AND ADDITIONAL TAX  
5           PAYABLE WITH RESPECT TO PREVIOUSLY DE-  
6           FERRED COMPENSATION.—

7           “(i) IN GENERAL.—If compensation is  
8           required to be included in gross income  
9           under subparagraph (A) for a taxable year,  
10          the tax imposed by this chapter for the  
11          taxable year of inclusion shall be increased  
12          by the sum of—

13                  “(I) the amount of interest deter-  
14                  mined under clause (ii), and

15                  “(II) an amount equal to 10 per-  
16                  cent of the compensation which is re-  
17                  quired to be included in gross income.

18          “(ii) INTEREST.—For purposes of  
19          clause (i), the interest determined under  
20          this clause for any taxable year is the  
21          amount of interest at the underpayment  
22          rate on the underpayments that would  
23          have occurred had the deferred compensa-  
24          tion been includible in gross income for the  
25          taxable year in which first deferred or, if

1 later, the first taxable year in which such  
2 deferred compensation is not subject to a  
3 substantial risk of forfeiture.

4 “(2) DISTRIBUTIONS.—

5 “(A) IN GENERAL.—The requirements of  
6 this paragraph are met if the plan provides that  
7 compensation deferred under the plan may not  
8 be distributed earlier than—

9 “(i) except as provided in subpara-  
10 graph (B)(i), separation from service (as  
11 determined by the Secretary),

12 “(ii) the date the participant becomes  
13 disabled (within the meaning of subpara-  
14 graph (C)),

15 “(iii) death,

16 “(iv) a specified time (or pursuant to  
17 a fixed schedule) specified under the plan  
18 as of the date of the deferral of such com-  
19 pensation,

20 “(v) to the extent provided by the  
21 Secretary, a change in the ownership or ef-  
22 fective control of the corporation, or in the  
23 ownership of a substantial portion of the  
24 assets of the corporation, or

1 “(vi) the occurrence of an unforesee-  
2 able emergency.

3 “(B) SPECIAL RULES.—

4 “(i) SEPARATION FROM SERVICE OF  
5 SPECIFIED EMPLOYEES.—In the case of  
6 specified employees, the requirement of  
7 subparagraph (A)(i) is met only if, except  
8 in the case of death, distributions may not  
9 be made earlier than 6 months after the  
10 date of separation from service. For pur-  
11 poses of the preceding sentence, a specified  
12 employee is a key employee (as defined in  
13 section 416(i) without regard to paragraph  
14 (5) thereof) of a corporation the stock in  
15 which is publicly traded on an established  
16 securities market or otherwise.

17 “(ii) CHANGES IN OWNERSHIP OR  
18 CONTROL.—In the case of a participant  
19 who is subject to the requirements of sec-  
20 tion 16(a) of the Securities Exchange Act  
21 of 1934, the requirement of subparagraph  
22 (A)(v) is met only if, except in the case of  
23 death, distributions may not be made ear-  
24 lier than 1 year after the date of the  
25 change in ownership or effective control.

1 “(iii) UNFORESEEABLE EMER-  
2 GENCY.—For purposes of subparagraph  
3 (A)(vi)—

4 “(I) IN GENERAL.—The term  
5 ‘unforeseeable emergency’ means a se-  
6 vere financial hardship to the partici-  
7 pant or beneficiary resulting from an  
8 illness or accident of the participant  
9 or beneficiary, the participant’s or  
10 beneficiary’s spouse, or the partici-  
11 pant’s or beneficiary’s dependent (as  
12 defined in section 152(a)), loss of the  
13 participant’s or beneficiary’s property  
14 due to casualty, or other similar ex-  
15 traordinary and unforeseeable cir-  
16 cumstances arising as a result of  
17 events beyond the control of the par-  
18 ticipant or beneficiary.

19 “(II) LIMITATION ON DISTRIBUTI-  
20 TIONS.—The requirement of subpara-  
21 graph (A)(vi) is met only if, as deter-  
22 mined under regulations of the Sec-  
23 retary, the amounts distributed with  
24 respect to an emergency do not exceed  
25 the amounts necessary to satisfy such

1 emergency plus amounts necessary to  
2 pay taxes reasonably anticipated as a  
3 result of the distribution, after taking  
4 into account the extent to which such  
5 hardship is or may be relieved  
6 through reimbursement or compensa-  
7 tion by insurance or otherwise or by  
8 liquidation of the participant's or  
9 beneficiary's assets (to the extent the  
10 liquidation of such assets would not  
11 itself cause severe financial hardship).

12 “(C) DISABLED.—For purposes of sub-  
13 paragraph (A)(ii), a participant shall be consid-  
14 ered disabled if the participant—

15 “(i) is unable to engage in any sub-  
16 stantial gainful activity by reason of any  
17 medically determinable physical or mental  
18 impairment which can be expected to result  
19 in death or can be expected to last for a  
20 continuous period of not less than 12  
21 months, or

22 “(ii) is, by reason of any medically de-  
23 terminable physical or mental impairment  
24 which can be expected to result in death or  
25 can be expected to last for a continuous

1 period of not less than 12 months, receiv-  
2 ing income replacement benefits for a pe-  
3 riod of not less than 3 months under an  
4 accident and health plan covering employ-  
5 ees of the participant's employer.

6 “(3) INVESTMENT OPTIONS.—The requirements  
7 of this paragraph are met if—

8 “(A) in the case of a plan that provides  
9 participants with the opportunity to elect in-  
10 vestment options—

11 “(i) changes to investments may not  
12 be made more frequently than every 3  
13 months,

14 “(ii) no more than 8 investment op-  
15 tions are available at any time,

16 “(iii) a brokerage window is not a per-  
17 missible option, and

18 “(iv) changes to investment options  
19 may not be made during a blackout period  
20 (within the meaning of section 101(i)(7) of  
21 the Employee Retirement Income Security  
22 Act of 1974, and

23 “(B) the plan does not provide a rate of  
24 return greater than a market rate of return, as  
25 determined by the Secretary.

1           “(4) ACCELERATION OF BENEFITS.—The re-  
2           quirements of this paragraph are met if the plan  
3           does not permit the acceleration of the time or  
4           schedule of any payment under the plan, except as  
5           provided by the Secretary in regulations.

6           “(5) ELECTIONS.—

7                 “(A) IN GENERAL.—The requirements of  
8                 this paragraph are met if the requirements of  
9                 subparagraphs (B) and (C) are met.

10                “(B) INITIAL DEFERRAL DECISION.—The  
11                requirements of this subparagraph are met if  
12                the plan provides that compensation for services  
13                performed during a taxable year may be de-  
14                ferred at the participant’s election only if the  
15                election to defer such compensation is made  
16                during the preceding taxable year or at such  
17                other time as provided in regulations. In the  
18                case of the first year in which a participant be-  
19                comes eligible to participate in the plan, such  
20                election may be made with respect to services to  
21                be performed subsequent to the election within  
22                30 days after the date the participant becomes  
23                eligible to participate in such plan. In the case  
24                of any performance-based compensation based  
25                on services performed over a period of at least



1 12 months, such election may be made no later  
2 than 6 months before the end of the period.

3 “(C) CHANGES IN TIME AND FORM OF DIS-  
4 TRIBUTION.—The requirements of this subpara-  
5 graph are met if, in the case of a plan which  
6 permits under a subsequent election a delay in  
7 a payment or a change in the form of  
8 payment—

9 “(i) the plan requires that such elec-  
10 tion may not take effect until at least 12  
11 months after the date on which the elec-  
12 tion is made,

13 “(ii) in the case an election related to  
14 a payment not described in clause (ii), (iii),  
15 or (vi) of paragraph (2)(A), the plan re-  
16 quires that the first payment with respect  
17 to which such election is made be deferred  
18 for a period of not less than 5 years from  
19 the date such payment would otherwise  
20 have been made, and

21 “(iii) the plan requires that any elec-  
22 tion related to a payment described in  
23 paragraph (2)(A)(iv) may not be made less  
24 than 12 months prior to the date of the

1 first scheduled payment under such para-  
2 graph.

3 A plan shall be treated as failing to meet the  
4 requirements of this subparagraph if the plan  
5 permits more than 1 subsequent election to  
6 delay any payment.

7 “(b) RULES RELATING TO FUNDING.—

8 “(1) OFFSHORE PROPERTY IN A TRUST.—In  
9 the case of assets set aside (directly or indirectly) in  
10 a trust (or other arrangement determined by the  
11 Secretary) for purposes of paying deferred com-  
12 pensation under a nonqualified deferred compensa-  
13 tion plan, such assets shall be treated for purposes  
14 of section 83 as property transferred in connection  
15 with the performance of services whether or not such  
16 assets are available to satisfy claims of general  
17 creditors—

18 “(A) at the time set aside if such assets  
19 (or such trust or other arrangement) are lo-  
20 cated outside of the United States, or

21 “(B) at the time transferred if such assets  
22 (or such trust or other arrangement) are subse-  
23 quently transferred outside of the United  
24 States.

1       This paragraph shall not apply to assets located in  
2       a foreign jurisdiction if substantially all of the serv-  
3       ices to which the nonqualified deferred compensation  
4       relates are performed in such jurisdiction.

5               “(2) EMPLOYER’S FINANCIAL HEALTH.—In the  
6       case of a nonqualified deferred compensation plan,  
7       there is a transfer of property within the meaning  
8       of section 83 as of the earlier of—

9               “(A) the date on which the plan first pro-  
10       vides that assets will become restricted to the  
11       provision of benefits under the plan in connec-  
12       tion with a change in the employer’s financial  
13       health, or

14              “(B) the date on which assets are so re-  
15       stricted.

16              “(3) INCOME INCLUSION FOR OFFSHORE  
17       TRUSTS AND EMPLOYER’S FINANCIAL HEALTH.—For  
18       each taxable year that assets treated as transferred  
19       under this subsection remain set aside in a trust or  
20       other arrangement subject to paragraph (1) or (2),  
21       any increase in value in, or earnings with respect to,  
22       such assets shall be treated as an additional transfer  
23       of property under this subsection (to the extent not  
24       previously included in income).

1           “(4) INTEREST ON TAX LIABILITY PAYABLE  
2       WITH RESPECT TO TRANSFERRED PROPERTY.—

3           “(A) IN GENERAL.—If amounts are re-  
4       quired to be included in gross income by reason  
5       of paragraph (1) or (2) for a taxable year, the  
6       tax imposed by this chapter for such taxable  
7       year shall be increased by the sum of—

8           “(i) the amount of interest determined  
9       under subparagraph (B), and

10          “(ii) an amount equal to 10 percent of  
11       the amounts required to be included in  
12       gross income.

13          “(B) INTEREST.—For purposes of sub-  
14       paragraph (A), the interest determined under  
15       this subparagraph for any taxable year is the  
16       amount of interest at the underpayment rate on  
17       the underpayments that would have occurred  
18       had the amounts so required to be included in  
19       gross income by paragraph (1) or (2) been in-  
20       cludible in gross income for the taxable year in  
21       which first deferred or, if later, the first taxable  
22       year in which such amounts are not subject to  
23       a substantial risk of forfeiture.

24          “(c) NO INFERENCE ON EARLIER INCOME INCLU-  
25       SION.—Nothing in this section shall be construed to pre-

1 vent the inclusion of amounts in gross income under any  
2 other provision of this chapter or any other rule of law  
3 earlier than the time provided in this section. Any amount  
4 included in gross income under this section shall not be  
5 required to be included in gross income under any other  
6 provision of this chapter or any other rule of law later  
7 than the time provided in this section.

8 “(d) OTHER DEFINITIONS AND SPECIAL RULES.—  
9 For purposes of this section—

10 “(1) NONQUALIFIED DEFERRED COMPENSA-  
11 TION PLAN.—The term ‘nonqualified deferred com-  
12 pensation plan’ means any plan that provides for the  
13 deferral of compensation, other than—

14 “(A) a qualified employer plan,

15 “(B) any bona fide vacation leave, sick  
16 leave, compensatory time, disability pay, or  
17 death benefit plan, and

18 “(C) any qualified stock appreciation  
19 rights plan.

20 For purposes of subparagraph (C), a qualified stock  
21 appreciation rights plan means any plan under  
22 which stock appreciation rights are granted which  
23 entitle the employee to a cash payment equal to the  
24 excess of the fair-market value of one share of com-  
25 mon stock of the employer corporation on the date

1 of the exercise of the rights over the value of such  
2 share on the date such rights were granted to the  
3 employee. The preceding sentence shall not apply to  
4 a plan unless the plan provides that the date of the  
5 exercise of any right cannot be more than 5 years  
6 after the date such right is granted, the plan pro-  
7 vides that the cash payment must be made within 60  
8 days of the date of the exercise, the plan provides  
9 that the value of the corporation's stock is deter-  
10 mined on the basis of an independent appraisal per-  
11 formed within 12 months of the date for which the  
12 value is being determined, no member of any con-  
13 trolled group of corporations which includes the em-  
14 ployer corporation maintaining the plan has stock  
15 which is publicly traded, and the plan meets such  
16 other requirements as the Secretary may prescribe.

17 “(2) QUALIFIED EMPLOYER PLAN.—The term  
18 ‘qualified employer plan’ means—

19 “(A) any plan, contract, pension, account,  
20 or trust described in subparagraph (A) or (B)  
21 of section 219(g)(5) (without regard to sub-  
22 paragraph (A)(iii)), and

23 “(B) any eligible deferred compensation  
24 plan (within the meaning of section 457(b)).

1       Such term does not include any plan described in  
2       section 415(m).

3               “(3) PLAN INCLUDES ARRANGEMENTS, ETC.—  
4       The term ‘plan’ includes any agreement or arrange-  
5       ment, including an agreement or arrangement that  
6       includes one person.

7               “(4) SUBSTANTIAL RISK OF FORFEITURE.—The  
8       rights of a person to compensation are subject to a  
9       substantial risk of forfeiture if such person’s rights  
10      to such compensation are conditioned upon the fu-  
11      ture performance of substantial services by any indi-  
12      vidual.

13              “(5) TREATMENT OF EARNINGS.—References to  
14      deferred compensation shall be treated as including  
15      references to income (whether actual or notional) at-  
16      tributable to such compensation or such income.

17              “(6) EXCEPTION FOR NONELECTIVE DEFERRED  
18      COMPENSATION.—This section shall not apply to any  
19      nonelective deferred compensation to which section  
20      457 does not apply by reason of section 457(e)(12),  
21      but only if such compensation is provided under a  
22      nonqualified deferred compensation plan which was  
23      in existence on May 1, 2004, and which was pro-  
24      viding nonelective deferred compensation described  
25      in section 457(e)(12) on such date. If, after May 1,

1       2004, a plan described in the preceding sentence  
2       adopts a plan amendment which provides a material  
3       change in the classes of individuals eligible to par-  
4       ticipate in the plan, this paragraph shall not apply  
5       to any nonelective deferred compensation provided  
6       under the plan on or after the date of the adoption  
7       of the amendment.

8       “(e) REGULATIONS.—The Secretary shall prescribe  
9       such regulations as may be necessary or appropriate to  
10      carry out the purposes of this section, including  
11      regulations—

12           “(1) providing for the determination of  
13           amounts of deferral in the case of a nonqualified de-  
14           ferred compensation plan which is a defined benefit  
15           plan,

16           “(2) relating to changes in the ownership and  
17           control of a corporation or assets of a corporation  
18           for purposes of subsection (a)(2)(A)(v),

19           “(3) exempting arrangements from the applica-  
20           tion of subsection (b) if such arrangements will not  
21           result in an improper deferral of United States tax  
22           and will not result in assets being effectively beyond  
23           the reach of creditors,

24           “(4) defining financial health for purposes of  
25           subsection (b)(2),



1 “(5) disregarding a substantial risk of for-  
2 feiture in cases where necessary to carry out the  
3 purposes of this section, and

4 “(6) defining a market rate of return for pur-  
5 poses of subsection (a)(3).”

6 (b) APPLICATION OF GOLDEN PARACHUTE PAYMENT  
7 PROVISIONS.—Section 280G of such Code (relating to  
8 golden parachute payments) is amended by redesignating  
9 subsection (e) as subsection (f) and by inserting after sub-  
10 section (d) the following new subsection:

11 “(e) SPECIAL RULES FOR CERTAIN PAYMENTS FROM  
12 NONQUALIFIED DEFERRED COMPENSATION PLANS.—

13 “(1) IN GENERAL.—Notwithstanding any other  
14 provision of this section, an applicable payment shall  
15 be treated as an excess parachute payment for pur-  
16 poses of this section and section 4999.

17 “(2) COORDINATION WITH OTHER PAY-  
18 MENTS.—

19 “(A) APPLICABLE PAYMENTS WHICH ARE  
20 PARACHUTE PAYMENTS.—If any applicable pay-  
21 ment is a parachute payment (determined with-  
22 out regard to subsection (b)(2)(A)(ii))—

23 “(i) except as provided in paragraph  
24 (4), this section shall be applied to such

1 payment in the same manner as if this  
2 subsection had not been enacted, and

3 “(ii) if such application results in an  
4 excess parachute payment, any tax under  
5 section 4999 on the excess parachute pay-  
6 ment shall be in addition to the tax im-  
7 posed by reason of paragraph (1).

8 “(B) APPLICABLE PAYMENTS WHICH ARE  
9 NOT PARACHUTE PAYMENTS.—An applicable  
10 payment not described in subparagraph (A)  
11 shall be taken into account in determining  
12 whether any payment described in subpara-  
13 graph (A) or any payment which is not an ap-  
14 plicable payment is a parachute payment under  
15 subsection (b)(2).

16 “(3) APPLICABLE PAYMENT.—For purposes of  
17 this subsection, the term ‘applicable payment’ means  
18 any distribution (including any distribution treated  
19 as a parachute payment without regard to this sub-  
20 section) from a nonqualified deferred compensation  
21 plan (as defined in section 409A(d)) which is  
22 made—

23 “(A) to a participant who is subject to the  
24 requirements of section 16(a) of the Securities  
25 Exchange Act of 1934, and

1           “(B) during the 1-year period following a  
2           change in the ownership or effective control of  
3           the corporation or in the ownership of a sub-  
4           stantial portion of the assets of the corporation.  
5       Such terms shall not include any distribution by rea-  
6       son of the death of the participant or the participant  
7       becoming disabled (within the meaning of section  
8       409A(a)(2)(C)).

9           “(4) NO DOUBLE COUNTING.—Under regula-  
10          tions, proper adjustments shall be made in the appli-  
11          cation of this subsection to prevent a deduction from  
12          being disallowed more than once.”.

13       (c) TREATMENT OF DEFERRED AMOUNTS.—

14           (1) W-2 FORMS.—

15           (A) IN GENERAL.—Subsection (a) of sec-  
16          tion 6051 (relating to receipts for employees) is  
17          amended by striking “and” at the end of para-  
18          graph (11), by striking the period at the end of  
19          paragraph (12) and inserting “, and”, and by  
20          inserting after paragraph (12) the following  
21          new paragraph:

22           “(13) the total amount of annual deferrals  
23          under a nonqualified deferred compensation plan  
24          (within the meaning of section 409A(d)).”.

1 (B) THRESHOLD.—Subsection (a) of sec-  
2 tion 6051 is amended by adding at the end the  
3 following: “In the case of the amounts required  
4 to be shown by paragraph (13), the Secretary  
5 may (by regulation) establish a minimum  
6 amount of deferrals below which paragraph  
7 (13) does not apply.”.

8 (2) WAGE WITHHOLDING.—Section 3401(a)  
9 (defining wages) is amended by striking “or” at the  
10 end of paragraph (21), by striking the period at the  
11 end of paragraph (22), and by inserting after para-  
12 graph (22) the following:

13 “(23) any amount required to be included in  
14 gross income of an employee under section 409A.”

15 (3) OTHER REPORTING.—Section 6041 (relat-  
16 ing to information at source) is amended by adding  
17 at the end the following new subsection:

18 “(g) NONQUALIFIED DEFERRED COMPENSATION.—  
19 Subsection (a) shall apply to any amount paid to any per-  
20 son which is required to be included in gross income under  
21 section 409A and which is not treated as wages under sec-  
22 tion 3401(a)(23).”

23 (d) CONFORMING AND CLERICAL AMENDMENTS.—

24 (1) Section 414(b) is amended by inserting  
25 “409A,” after “408(p),”.

1           (2) Section 414(c) is amended by inserting  
2           “409A,” after “408(p),”.

3           (3) The table of sections for such subpart A is  
4           amended by adding at the end the following new  
5           item:

                  “Sec. 409A. Inclusion in gross income of deferred compensation  
                                  under nonqualified deferred compensation plans.”.

6           (e) EFFECTIVE DATE.—

7           (1) IN GENERAL.—Except as otherwise pro-  
8           vided in this subsection, the amendments made by  
9           this section shall apply to amounts deferred in tax-  
10          able years beginning after December 31, 2004.

11          (2) EXCEPTION FOR CERTAIN INDIVIDUALS.—

12          In the case of an individual—

13                  (A) who is not subject to section 16(a) of  
14                  the Securities Exchange Act of 1934, and

15                  (B) with respect to whom the amounts de-  
16                  ferred in any taxable year beginning in 2005 do  
17                  not exceed the highest amount deferred by the  
18                  individual for any taxable year in the 3 consecu-  
19                  tive taxable year period beginning with the tax-  
20                  payer’s last taxable year beginning before 2005,  
21                  the amendments made by this section shall  
22                  apply to amounts deferred in taxable years  
23                  beginning after December 1, 2005.

24          (3) SPECIAL RULES.—

1 (A) EARNINGS.—The amendments made  
2 by this section shall apply to earnings on de-  
3 ferred compensation only to the extent that  
4 such amendments apply to such compensation.

5 (B) MATERIAL MODIFICATIONS.—For pur-  
6 poses of this subsection, amounts deferred in  
7 taxable years beginning after December 31,  
8 2004 (2005 in the case of amounts to which  
9 paragraph (2) applies) shall be treated as  
10 amounts deferred in a taxable year beginning  
11 after such date if the plan under which the de-  
12 ferral is made is materially modified after the  
13 date of the enactment of this Act, unless such  
14 modification is required pursuant to the guid-  
15 ance issued under subsection (g).

16 (f) GUIDANCE RELATING TO CHANGE OF OWNER-  
17 SHIP OR CONTROL.—Not later than 90 days after the date  
18 of the enactment of this Act, the Secretary of the Treasury  
19 shall issue guidance on what constitutes a change in own-  
20 ership or effective control, and what constitutes a market  
21 rate of return for purposes of section 409A of the Internal  
22 Revenue Code of 1986, as added by this section.

23 (g) GUIDANCE RELATING TO TERMINATION OF CER-  
24 TAIN EXISTING ARRANGEMENTS.—Not later than 90 days  
25 after the date of the enactment of this Act, the Secretary

1 of the Treasury shall issue guidance providing a limited  
2 period during which an individual participating in a non-  
3 qualified deferred compensation plan adopted on or before  
4 December 31, 2004, may, without violating the require-  
5 ments of paragraphs (2), (3), (4), and (5) of section  
6 409A(a) of the Internal Revenue Code of 1986 (as added  
7 by this section), terminate participation or cancel an out-  
8 standing deferral election (or modify an outstanding defer-  
9 ral election in compliance with section 409A of such Code,  
10 as so added) with regard to amounts earned after Decem-  
11 ber 31, 2004, if such amounts are includible in income  
12 as earned.

13 **SEC. 672. PROHIBITION ON DEFERRAL OF GAIN FROM THE**  
14 **EXERCISE OF STOCK OPTIONS AND RE-**  
15 **STRICTED STOCK GAINS THROUGH DE-**  
16 **FERRED COMPENSATION ARRANGEMENTS.**

17 (a) IN GENERAL.—Section 83 (relating to property  
18 transferred in connection with performance of services) is  
19 amending by adding at the end the following new sub-  
20 section:

21 “(i) PROHIBITION ON ADDITIONAL DEFERRAL  
22 THROUGH DEFERRED COMPENSATION ARRANGE-  
23 MENTS.—If a taxpayer exchanges—

24 “(1) an option to purchase employer  
25 securities—

1                   “(A) to which subsection (a) applies, or  
2                   “(B) which is described in subsection  
3                   (e)(3), or  
4                   “(2) employer securities or any other property  
5           based on employer securities transferred to the tax-  
6           payer,  
7   for a right to receive future payments, then, notwith-  
8   standing any other provision of this title, there shall be  
9   included in gross income for the taxable year of the ex-  
10   change an amount equal to the present value of such right  
11   (or such other amount as the Secretary may by regulations  
12   specify). For purposes of this subsection, the term ‘em-  
13   ployer securities’ includes any security issued by the em-  
14   ployer.”.

15           (b) CONTROLLED GROUP RULES.—Section 414(t)(2)  
16   is amended by inserting “83(i),” after “79,”.

17           (c) EFFECTIVE DATE.—The amendments made by  
18   this section shall apply to any exchange after December  
19   31, 2004.