

Digest of Jobs and Growth Tax Relief Reconciliation Act of 2003

(P. L. No. 108-27; May 28, 2003)

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

CODE SECTION DESCRIPTION OF PROVISION

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

§ 1(f)(8)(A)	Acceleration of 15 percent individual income tax rate bracket expansion for married taxpayers filing joint returns – conforming amendment. Effective for taxable years beginning after December 31, 2002, and before January 1, 2005. Act §102(b)(1).
§ 1(f)(8)(B)	Acceleration of 15 percent individual income tax rate bracket expansion for married taxpayers filing joint returns . Increases the size of the 15-percent regular income tax rate bracket for joint returns to twice the width of the 15-percent regular income tax rate bracket for single returns for taxable years beginning in 2003 and 2004. Effective for taxable years beginning after December 31, 2002, and before January 1, 2005. Act §102(a).
§ 1(h)(1)(B)	Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement. Reduces the 10 and 20 percent rates on the adjusted net capital gain to five (or zero for taxable years beginning after December 31, 2007) and 15 percent, respectively. These lower rates apply to both the regular tax and the alternative minimum tax. The lower rates apply to assets held more than one year. Effective for taxable years ending on or after May 6, 2003, and beginning before January 1, 2009. For taxable years that include May 6, 2003, the lower rates apply to amounts properly taken into account for the portion of the year on or after that date. This generally has the effect of applying the lower rates to capital assets sold or exchanged (and installment payments received) on or after May 6, 2003. In the case of gain and loss taken into account by a pass-through entity, the date taken into account by the entity is the appropriate date for applying this rule. Act § 301(a)(1).
§ 1(h)(1)(C)	Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement. Reduces the 20 percent rates on the adjusted net capital gain to 15 percent. Effective tax years ending on or after May 6, 2003. Act § 301(a)(2)(A).
§ 1(h)(2)-(8)	Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement – conforming amendment. Effective tax years ending on or after May 6, 2003. Act § 301(b)(1)(B).
§ 1(h)(2)	Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement – conforming amendment. Effective tax years ending on or after May 6, 2003. Act § 301(b)(1)(A).

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- § 1(h)(3) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective tax years beginning after December 31, 2002. Act § 302(e)(1).
- § 1(h)(8)-(12) Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement – conforming amendment. Effective tax years ending on or after May 6, 2003. Act § 301(b)(1)(C).
- § 1(h)(9) Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement – conforming amendment. Effective tax years ending on or after May 6, 2003. Act § 301(b)(1)(A).
- 1(h)(11) Dividends of individuals taxed at capital gains rates. Effective tax years beginning after December 31, 2002. Act § 302(a).
- § 1(i)(1)(B) & (C) Acceleration of the increase in the taxable income levels for the 10 percent rate bracket. For 2003 and 2004, increases the taxable income level for the 10 percent regular income tax rate brackets for unmarried individuals from \$6,000 to \$7,000 and for married individuals filing jointly from \$12,000 to \$14,000. The taxable income levels for the 10 percent regular income tax rate bracket will be adjusted annually for inflation for taxable years beginning after December 31, 2003. For taxable years beginning after December 31, 2004, the taxable income levels for the 10-percent rate bracket will revert to the levels allowed under present law. Therefore, for 2005, 2006, and 2007, the levels will revert to \$6,000 for unmarried individuals and \$12,000 for married individuals filing jointly. Effective for taxable years beginning after December 31, 2002. Act §§ 104(a) & (b).
- § 1(i)(2) Acceleration of reduction in individual income tax rates. Accelerates the reductions in the regular income tax rates in excess of the 15-percent regular income tax rate that are scheduled for 2004 and 2006. Therefore, for 2003 and thereafter, the regular income tax rates, in excess of 15 percent, are 25 percent, 28 percent, 33 percent, and 35 percent. Effective for taxable years beginning after December 31, 2002. Act § 105(a).
- § 24(a)(2) Acceleration of increase in child tax credit. Tax years beginning after December 31, 2002. Act § 101(a).
- § 55(b)(3)(B) Reduction in capital gains rates for individuals; repeal of 5-year holding period requirements. Reduces the 10 percent rate on the adjusted net capital gain to five (or zero for taxable years beginning after December 31, 2007). The lower rate applies to both the regular tax and the alternative minimum tax. Effective tax years ending on or after May 6, 2003. Act § 301(a)(1).
- § 55(d)(1) Alternative minimum tax exemption. Increases the AMT exemption amount for married taxpayers filing a joint return and surviving spouses to \$58,000, and for unmarried taxpayers to \$40,250 for taxable years beginning in 2003 and 2004. Effective for taxable years beginning after December 31, 2002. Act § 106.
- § 57(a)(7) Reduction in capital gains rates for individuals; repeal of 5-year holding period requirements. For dispositions of small business stock on or after May 6, 2003, only 7 percent of the 50 percent exclusion is treated as a tax preference item when computing alternative minimum taxable income. Effective for dispositions on or after May 6, 2003. Act § 301(b)(3).
- § 63(c)(7) Standard deduction marriage penalty relief. Increases the basic standard deduction amount for joint returns to twice the basic standard deduction amount for single returns effective for 2003 and 2004. For taxable years beginning after 2004, the applicable percentages will revert

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- to those allowed under present law, as described above. Effective for taxable years beginning after December 31, 2002, and before January 1, 2005. Act § 103(a).
- § 163(d)(4)(B) Dividends of individuals taxed at capital gain rates – exclusion of dividends from investment income. Effective for tax years ending after May 5, 2003. Act § 302(b).
- § 168(k)(2)(A) Increase and extension of bonus depreciation. Provides an additional first-year depreciation deduction equal to 50-percent of the adjusted basis of qualified property placed in service before January 1, 2005. Provides that the increase on the amount of depreciation deductions allowed with respect to certain passenger automobiles (sec. 280F of the Code) in the first year is \$7,650 for automobiles that qualify. Effective for taxable years ending after May 5, 2003. Act § 201(b)(2).
- § 168(k)(2)(B) Increase and extension of bonus depreciation – extension of certain dates for 30 percent bonus depreciation property – portion of basis taken into account. Effective tax years ending after May 5, 2003. Act § 201(b)(1)(A).
- § 168(k)(2)(C) Increase and extension of bonus depreciation – extension of certain dates for 30 percent bonus depreciation property – election. Effective tax years ending after May 5, 2003. Act § 201(b)(3).
- § 168(k)(2)(D) Increase and extension of bonus depreciation – extension of certain dates for 30 percent bonus depreciation property – portion of basis taken into account. Effective tax years ending after May 5, 2003. Act § 201(b)(1)(A).
- § 168(k)(4) Increase and extension of bonus depreciation. Effective tax years ending after May 5, 2003. Act § 201(a).
- § 168(k) Increase and extension of bonus depreciation – conforming amendment. Effective tax years ending after May 5, 2003. Act § 201(c)(1).
- § 179(b)(1) Increased expensing for small business. Provides that the maximum dollar amount that may be deducted under section 179 is increased to \$100,000 for property placed in service in taxable years beginning in 2003, 2004, and 2005. In addition, the \$200,000 amount is increased to \$400,000 for property placed in service in taxable years beginning in 2003, 2004, and 2005. Effective tax years beginning after December 31, 2002. Act § 202(a).
- § 179(b)(2) Increased expensing for small business – increase in qualifying investment at which phaseout begins. Effective for taxable years beginning after December 31, 2002. Act § 202.
- § 179(b)(5) Increased expensing for small business. Adjustment of dollar limit and phaseout threshold for inflation. The dollar limitations are indexed annually for inflation for taxable years beginning after 2003 and before 2006. Effective for taxable years beginning after December 31, 2002. Act § 202(D).
- § 179(c)(2) Increased expensing for small business. With respect to a taxable year beginning after 2002 and before 2006, the provision permits taxpayers to make or revoke expensing elections on amended returns without the consent of the Commissioner. Effective for taxable years beginning after December 31, 2002. Act § 202(e).
- § 179(d)(1) Increased expensing for small business. The provision also includes off-the-shelf computer software placed in service in a taxable year beginning in 2003, 2004, and 2005, as qualifying

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- property. Effective for taxable years beginning after December 31, 2002. Act § 202(c).
- § 301(f)(4) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(c)(2).
- § 306(a)(1)(D) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(3).
- § 338(h)(14) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(B).
- § 341 Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(A).
- § 467(c)(5)(C) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(B).
- § 531 Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(5).
- § 541 Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(6).
- § 584(c) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(7).
- § 702(a)(5) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(c)(1).
- § 854(a) Dividends of individuals taxed at capital gains rates – treatment of dividends from regulated investments companies. Effective tax years ending after December 31, 2002, generally. Act § 302(c)(1).
- § 854(b)(1)(B) & (C) Dividends of individuals taxed at capital gains rates – treatment of dividends from regulated investments companies. Effective tax years ending after December 31, 2002, generally. Act § 302(c)(2).
- § 854(b)(1)(C) Dividends of individuals taxed at capital gains rates – treatment of dividends from regulated investments companies. Effective tax years ending after December 31, 2002, generally. Act § 302(c)(3).
- § 854(b)(2) Dividends of individuals taxed at capital gains rates – treatment of dividends from regulated investments companies. Effective tax years ending after December 31, 2002, generally. Act § 302(c)(4).
- § 854(b)(5) Dividends of individuals taxed at capital gains rates – treatment of dividends from regulated investments companies. Effective tax years ending after December 31, 2002, generally. Act § 302(c)(5).
- § 857(c) Dividends of individuals taxed at capital gains rates – treatment of dividends from real estate investment trusts. Effective tax years ending after December 31, 2002, generally. Act §

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- 302(c)(Act § 302(d).
- § 1255(b)(2) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(B).
- § 1257(d) Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(B).
- §1400L(b)(2)(C)(i) Increase and extension of bonus depreciation – conforming amendment. Effective tax years ending after May 5, 2003. Act § 201(c)(2).
- §1445(e)(1) Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement. Reduces the 20 percent rates on the adjusted net capital gain to 15 percent. Effective tax years ending on or after May 6, 2003. Act § 301(a)(2)(C).
- § 6429 Child tax credit – advance payment of portion of increase credit in 2003. . Increased to \$1,000 for 2003 and 2004. After 2004, the credit reverts to the levels provided under present law. For 2003, the increased amount of the child credit will be paid in advance beginning in July 2003, on the basis of information on each taxpayer’s 2002 return filed in 2003. Effective for taxable years beginning after December 31, 2002, and before January 1, 2005. Act § 101(b)(1).
- § 7518(g)(6)(A) Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement. Reduces the 20 percent rates on the adjusted net capital gain to 15 percent. Effective tax years ending on or after May 6, 2003. Act § 301(a)(2)(D).
- Non-code Child tax credit – advance payment of portion of increase credit in 2003 – clerical amendment. Effective upon date of enactment (May 28, 2003). Act § 101(b)(2).
- Non-code Acceleration of 15 percent individual income tax rate bracket expansion for married taxpayers filing joint returns – conforming amendment. Effective tax years beginning after December 31, 2002. Act § 102(b)(2).
- Non-code Acceleration of increase in standard deduction for married taxpayers filing joint returns – conforming amendment. Effective tax years beginning after December 31, 2002. Act § 103(b).
- Non-code Application of EGTRRA sunset to this title. Effective upon date of enactment (May 28, 2003). Act § 107.
- Non-code Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement. Reduces the 20 percent rates on the adjusted net capital gain to 15 percent (Merchant Marine Act). Effective tax years ending on or after May 6, 2003. Act § 301(a) (2) (E).
- Non-code Reduction of capital gains rates for individuals; repeal of 5-year holding period requirement – transitional rules for taxable years that include May 6, 2003. Effective tax years ending on or after May 6, 2003. Act § 301(c)(1)-(6).
- Non-code Dividends of individuals taxed at capital gains rates – conforming amendment. Effective for tax years beginning after December 31, 2002. Act § 302(e)(4)(B).

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- Non-code Sunset of title. Effective upon date of enactment (May 28, 2003). Act § 303.
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – permitting maintenance of fiscal year 2002 FMAP for last 2 calendar quarters of fiscal year 2003. Effective upon date of enactment (May 28, 2003) Act § 401(a)(1).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – permitting maintenance of fiscal year 2003 FMAP for first 3 calendar quarters of fiscal year 2004. Effective upon date of enactment (May 28, 2003) Act § 401(a)(2).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – general 2.95 percentage point increase for last 2 calendar quarters of 2003 and first 3 calendar quarters of 2004. Effective upon date of enactment (May 28, 2003). Act § 401(a)(3).
- Non-code Temporary state fiscal relief – \$10,000,000,000 for a temporary increase of the Medicaid FMAP – increase in cap on Medicaid payments to territories. Effective upon date of enactment (May 28, 2003). Act § 401(a)(4).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – scope of application. Effective upon date of enactment (May 28, 2003) Act § 401(a)(5).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – state eligibility. Effective upon date of enactment (May 28, 2003) Act § 401(a)(6)(A).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – state eligibility – state reinstatement of eligibility permitted. Effective upon date of enactment (May 28, 2003) Act § 401(a)(6)(B).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – state eligibility – rule of construction. Effective upon date of enactment (May 28, 2003). Act § 401(a)(6)(C).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – requirement of certain states. Effective upon date of enactment (May 28, 2003). Act § 401(a)(7).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – definitions – FMAP. Effective upon date of enactment (May 28, 2003). Act § 401(a)(8)(A).
- Non-code Temporary state fiscal relief - \$10,000,000,000 for a temporary increase of the Medicaid FMAP – definitions – state. Effective upon date of enactment (May 28, 2003). Act § 401(a)(8)(B).
- Non-code Temporary state fiscal relief – \$10,000,000,000 for a temporary increase of the Medicaid FMAP – repeal. Effective upon date of enactment (May 28, 2003). Act § 401(b).
- Non-code Time for payment of corporate estimated taxes. Effective upon date of enactment (May 28, 2003). Act § 501.

Digest of the Military Family Tax Relief Act of 2003

(P. L. No. 108-121, Nov. 11, 2003)

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

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

§ 62, § 162	Above-the-Line Deduction for Overnight Travel Expenses of National Guard and Reserve Members. Provides an above-the-line deduction for the overnight transportation, meals and lodging expenses of National Guard and Reserve members who must travel more than 100 miles away from home and stay overnight to attend meetings. The maximum rate allowed for travel expenses authorized for employees of agencies under subchapter I of chapter 57 of 5 U.S.C. would be allowed as a deduction. Effective for amounts paid or incurred in taxable years beginning after December 31, 2002. Act § 109.
§§ 101, 692, 2201	Tax Relief and Assistance for Families of Space Shuttle Columbia Heroes. Extends the exclusion from income tax, the exclusion for death benefits, and the estate tax relief available under the Victims of Terrorism Tax Relief Act of 2001 to astronauts who lose their lives in the line of duty. Effective for any astronaut whose death occurs after December 31, 2002. Act § 110.
§ 121	Special Rule for Members of Uniformed Services or Foreign Service in Determining Exclusion of Gain from Sale of Principal Residence. Provides individuals and their spouses an election to suspend, for a maximum of ten years, the five-year test period for ownership and use during certain absences due to service in the Army, Navy, Air Force, Marine Corps, and Coast Guard, the commissioned corps of the National Oceanic and Atmospheric Administration, the commissioned corps of the Public Health Service (the uniformed services), and the U.S. Foreign Service. If the election is made, the five-year period ending on the date of the sale or exchange of a principal residence does not include any period of up to ten years during which the taxpayer or the taxpayer's spouse is on qualified official extended duty as a member of the uniformed services, or the Foreign Service. Qualified official extended duty is any period of extended duty while serving at a duty station at least 50 miles away from the taxpayer's principal residence or under orders requiring residence in government-furnished quarters. Extended duty is any period of duty under a call or order to such duty for a period of more than 90 days or for an indefinite period. The election may be made with respect to only one property for a suspension period, and may be revoked at any time. Effective for sales or exchanges after May 6, 1997, with the statute of limitations on refund claims suspended for a one-year period. Act § 101.
§ 132	Exclusion for Amounts Received Under Department of Defense Homeowners Assistance Program. Adds to the list of qualified fringe benefits exempt from gross income amounts received under the Department of Defense Homeowners Assistance Program ("HAP"). Amounts received under HAP would not be considered wages for FICA tax purposes and the excludible amount would be limited to the reduction in the fair market value of property.

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Effective for payments made after the date of enactment. Act § 103.

- § 134 Treatment of Death Gratuities Payable with Respect to Deceased Members of the Armed Forces. Extends the exclusion from gross income to any adjustment to the amount of the death gratuity payable with respect to the death of certain members of the Armed Services on active duty, inactive duty training, or engaged in authorized travel. Also increases the amount of the exclusion from \$6,000 to \$12,000. Effective with respect to deaths occurring after September 10, 2001. Act § 102.
- § 134 Clarification of the Treatment of Certain Dependent Care Assistance Programs. Provides that dependent care assistance provided under a dependent care assistance program (as in effect on the date of enactment) for a member of the uniformed services by reason of such member's status or service as a member of the uniformed services is excludible from gross income as a qualified military benefit subject to the present-law rules. The uniformed services include: (1) the Armed Forces; (2) the commissioned corps of the National Oceanic and Atmospheric Administration; and (3) the commissioned corps of the public health service. Amounts received under the program are not considered wages for Federal Insurance Contribution Act (FICA) tax purposes. Effective for tax years beginning after December 31, 2002. Act § 106.
- § 501 Modification of Membership Requirement for Exemption from Tax for Certain Veterans' Organizations. Permits ancestors or lineal descendants of past or present members of the U.S. Armed Forces or of cadets to qualify as members for purposes of the "substantially all" test of §501(c)(19). Does not change the requirement that 75% of the organization's members must be past or present members of the U.S. Armed Forces. Effective for taxable years beginning after the date of the enactment. Act § 105.
- § 501 Suspension of Tax-Exempt Status of Terrorist Organizations. Suspends an organization's tax-exempt status for any period during which the organization is designated or identified by U.S. federal authorities as a terrorist organization or supporter of terrorism. Such an organization would be ineligible to apply for such status. Period of suspension runs from the date the organization is first designated or identified (or from the date of enactment of this subsection, whichever is later) to the date when the designations or identifications have been rescinded pursuant to the law or executive order under which the designation or identification was made. During the period of suspension, deduction for any contribution to a terrorist organization under §§170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), and 2522 are disallowed. Effective for designations made before, on or after the date of enactment. Act § 108.
- § 530(d)(4) Clarification Relating to Exception from Additional Tax on Certain Distributions from Qualified Tuition Programs, Etc. on Account of Attendance at Military Academy. Provides penalty-free withdrawals from Coverdell education savings accounts and qualified tuition programs made on account of the attendance of the beneficiary at the U.S. Military Academy, the U.S. Naval Academy, the U.S. Air Force Academy, the U.S. Coast Guard Academy, or the U.S. Merchant Marine Academy. The penalty-free withdrawal amount is limited to the costs of advanced education as defined in 10 U.S.C. §2005(e)(3), as in effect on the date of enactment, at such Academies. Effective for taxable years beginning after December 31, 2002. Act § 107.

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

- § 7508 Expansion of Combat Zone Filing Rules to Contingency Operations. Applies the special suspension of time period rules to persons deployed outside the United States away from the individual's permanent duty station while participating in an operation designated by the Secretary of Defense as a contingency operation or that becomes a contingency operation. A contingency operation would be defined as a military operation that is designated by the

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Secretary of Defense as an operation in which members of the Armed Forces are or may become involved in military actions, operations, or hostilities against an enemy of the United States or against an opposing military force, or results in the call or order to active duty of members of the uniformed services during a war or a national emergency declared by the President or Congress. Effective for any period for performing an act which has not expired before the date of enactment. Act § 104.

Non-Code

Extension of Customs User Fees. To offset the tax relief provided by the Act, the sunset date for customs user fees is extended from March 31, 2004 to March 1, 2005. Act § 201.

Digest of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (P. L. No. 108-173, Dec. 8, 2003)

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

<u>CODE SECTION</u>	<u>DESCRIPTION OF PROVISION</u>
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The following provision is operative for Hawaii income tax purposes.

§ 139A (new)	<i>Exclusion of federal drug subsidy for prescription drug plan sponsors.</i> The 2003 Medicare Act adds Sec. 1860D-22 to the Social Security Act. Under this provision, the Social Security Administration must provide subsidies to each sponsor of a qualified retiree prescription drug plan for qualified covered retirees under the plan. In general, these subsidy payments will equal 28% of a covered retiree's plan-related prescription drug costs greater than \$250 but not greater than \$5,000, adjusted annually by the percentage increase in Medicare per capita prescription drug costs. The Act provides that gross income does not include these subsidies. These changes apply for tax years ending after date of enactment of the 2003 Medicare Act. Act § 1202.
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The following provision is NOT operative for Hawaii income tax purposes.

§ 4980G (new)	<i>Excise tax for discriminatory HSA contributions.</i> For any employer who makes a contribution to any employee's HSA during a calendar year, a tax will be imposed on the employer's failure to make comparable contributions to the HSAs of all comparable participating employees for that calendar year. The employer will be subject to a 35% tax on the aggregate amount contributed by the employer to HSAs of the employer for that period. This change applies for tax years beginning after Dec. 31, 2003. Act § 1201(d)(4).
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The following provisions are operative for Hawaii income tax purposes.

§ 62	<i>Contributions to HSAs treated as above-the-line deductions.</i> The 2003 Medicare Act adds the deduction allowed for contributions to HSAs to the list of deductions used to determine adjusted gross income. Act § 1201(b).
§ 106(d)	<i>Exclusions from income and employment taxes provided for employer contributions to HSAs.</i> An eligible employee will be able to exclude amounts contributed by his employer to his HSA (within Code Sec. 223(b) limits). The amounts will be treated as employer-provided coverage for medical expenses under an accident or health plan, and won't be subject to FICA, FUTA, or income tax withholding. These changes apply for tax years beginning after Dec. 31, 2003. Act § 1201(d).

- § 125(d) *HSAs may be offered under cafeteria plans.* For tax years beginning after Dec. 31, 2003, the rule prohibiting cafeteria plans from including deferred compensation arrangements won't apply to extent of amounts that a covered employee may elect to have the employer pay as contributions to an HSA established on the employee's behalf. Act § 1201(i).
- § 220(f)(5) *Tax-free rollovers from Archer medical savings accounts (MSA) permitted.* For tax years beginning after Dec. 31, 2003, Archer MSA account holders are permitted to roll over balances in their accounts to HSAs within 60 days of distribution, tax-free. Effective for payments made after December 31, 2002. Act § 1201(a).
- § 223 *Creation of new health savings accounts.* Under Code § 223, the 2003 Medicare Act creates a new tax-exempt vehicle called the health savings account (HSA), to which tax-deductible contributions can be made under certain circumstances to pay "qualified medical expenses" of "eligible individuals." These new accounts will be subject to many of the rules that apply to IRAs, such as the rule permitting contributions for a year to be made until the unextended due date of the return. Effective for tax years beginning after Dec. 31, 2003. Act § 1201(a).
- § 223(b) Deduction limits for contributions made to new HSAs by, or on behalf of, eligible individuals. The amount allowable as a deduction for contributions to each eligible individual's HSA for a tax year cannot exceed the sum of the monthly limits for months during which he is an eligible individual. The monthly limit is one-twelfth of: (A) for self-only coverage, the lesser of the annual deductible or \$2,250; or (B) for family coverage, the lesser of the annual deductible for family coverage or \$4,500. These amounts will be adjusted for cost of living increases. Larger deductible contributions will be permitted for those who are age 55 before the close of the tax year, increased by an "additional contribution amount" of \$500 for 2004, increasing by \$100 increments for succeeding years until the extra amount is \$1,000 for 2009 and thereafter. Also, the monthly limit that would apply to an individual for any tax year is reduced (but not below zero) by the sum of (a) amounts contributed to the individual's Archer MSAs (but this limit doesn't apply to married taxpayers), and (b) excludable employer contributions to the individual's HSAs for the tax year (and this amount is not allowed as a deduction under Code Sec. 223(a)). Additionally, no deduction is allowed for an HSA contribution for any individual for whom the Code Sec. 151 personal exemption can be claimed by another taxpayer for the tax year. These changes apply for tax years beginning after Dec. 31, 2003. Act § 1202(b).
- § 223(e) *Tax-Exempt status of HSAs.* Under the 2003 Medicare Act, an HSA will be exempt from tax, unless it ceases to be an HSA. However, HSAs will be subject to taxes imposed by Code Sec. 511 on unrelated business income of charitable organizations. The 2003 Medicare Act provides for the tax-exempt treatment of HSAs for tax years beginning after Dec. 31, 2003. Act § 1201(a).
- § 223(f)(2), (3) & (4) Rules governing distributions for HSAs. Any amount paid or distributed out of an HSA used exclusively to pay the "qualified medical expenses" of any "account beneficiary" is not includible in the account beneficiary's gross income. But, any amount paid or distributed from an HSA that isn't used exclusively to pay the qualified medical expenses of the account beneficiary is included in the beneficiary's gross income. Additional rules govern the return of excess contributions, rollover contributions, distributions not used for qualified medical expenses, and transfers of an individual's interest in an HSA to a spouse or former spouse under a divorce or

separation instrument. These changes go in effect for tax years beginning after Dec. 31, 2003. Effective for tax years beginning after Dec. 31, 2003. Act § 1201(a).

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

- § 848(e) *Policy acquisition expenses of health savings account contracts need not be capitalized.* Under Code Sec. 848, HSA contracts will be added to the list of insurance contracts that are not “specified insurance contracts.” Insurance companies acquiring HSA accounts after Dec. 31, 2003 won't be required to capitalize their expenses. Act § 1201(h).
- § 3231(e) *Exclusions from income and employment taxes provided for employer contributions to HSAs.* An eligible employee will be able to exclude amounts contributed by his employer to his HSA (within Code Sec. 223(b) limits). The amounts will be treated as employer-provided coverage for medical expenses under an accident or health plan, and won't be subject to **FICA**. These changes apply for tax years beginning after Dec. 31, 2003. Act § 1201(d).
- §3306(b) *Exclusions from income and employment taxes provided for employer contributions to HSAs.* An eligible employee will be able to exclude amounts contributed by his employer to his HSA (within Code Sec. 223(b) limits). The amounts will be treated as employer-provided coverage for medical expenses under an accident or health plan, and won't be subject to **FUTA**. These changes apply for tax years beginning after Dec. 31, 2003. Act § 1201(d).
- § 3401(a) *Exclusions from income and employment taxes provided for employer contributions to HSAs.* An eligible employee will be able to exclude amounts contributed by his employer to his HSA (within Code Sec. 223(b) limits). The amounts will be treated as employer-provided coverage for medical expenses under an accident or health plan, and won't be subject to **income tax withholding**. These changes apply for tax years beginning after Dec. 31, 2003. Act § 1201(d).
- § 4973 *Excise tax for excess contributions to HSAs.* The 2003 Medicare Act expands the existing 6% excise tax to cover “excess contributions” made to HSAs. The excess tax will be equal to 6% of the cumulative amount of excess contributions that are not distributed to the contributor. This change applies for tax years beginning after Dec. 31, 2003. Act § 1201(e).
- § 4975 *Prohibited transactions.* The 2003 Medicare Act adds HSAs to the list of plans that are subject to the excise tax on prohibited transactions. Also, the Act further provides that an individual for whose benefit an HSA is established will be exempt from the prohibited excise tax for any transaction concerning his account if, with respect to the transaction, the account ceases to be an HSA account because of the application of Code Sec. 223(e)(2). This change applies for tax years beginning after Dec. 31, 2003 Act § 1201(f).
- § 6041 *Exception to Information Reporting Requirements Related to Certain Health Arrangements.* The Act provides an exception from the generally applicable information reporting provisions for payments for medical care made under either a flexible spending arrangement or a health reimbursement arrangement that is treated as employer-provided coverage. Effective for payments made after December 31,

2002. Act § 1203.

- § 6051 *Employer contributions to HSAs must appear on Form W-2.* The amount contributed to any HSA, for an employee, or his spouse, must be reported on the employee's Form W-2. This provision is generally effective for tax years beginning after Dec. 31, 2003. Act § 1201(d)(3).
- § 6103 *Mandatory IRS disclosure of tax return information to Health and Human Services.* Under Code Sec. 6103, the 2003 Medicare Act provides that the IRS must, on written request from the Secretary of Health and Human Services (HHS) in carrying out new Section 1860D-31 of the Social Security Act, disclose certain specified information about a taxpayer for the "applicable year" to officers, employees, and contractors of HHS. This change becomes effective after date of enactment of the 2003 Medicare Act. Act § 105.
- § 6103 *IRS disclosure of return information to Social Security Administration to facilitate post-2006 income-related reduction in the Medicare Part B premium subsidy.* Under the 2003 Medicare Act, after 2006, in order to facilitate the income-related reduction in Part B premium subsidy, upon written request from the Commissioner of Social Security, IRS will have to disclose certain specified information for taxpayers whose Medicare Part B premium may be subject to an adjustment under section 1839(i) of the Social Security Act. This change becomes effective after date of enactment of the 2003 Medicare Act. Act § 811(c).
- § 6103(l)(12) *Update of reporting requirements to reflect renaming of the "Health Care Financing Administration" as the "Centers for Medicare and Medicaid Services."* The 2003 Medicare Act updates the Code Sec. 6103 reporting requirements to reflect the renaming of the Health Care Financing Administration. The Social Security Administrator must now disclose certain information identifying specified Medicare beneficiaries who have received wages to the Administrator of the Centers for Medicare and Medicaid Services. This change becomes effective after date of enactment of the 2003 Medicare Act. Act § 900(e)(3).
- § 6693 *Penalty for failure to file HSA account reports.* Persons responsible for filing the HSA reports required under Code Sec. 223 will be subject to \$50-per-failure penalty for non-filing. The penalty will apply to HSA trustees who will be required to report to the IRS amounts of contributions and distributions to IRS. This change is effective for tax years beginning after Dec. 31, 2003. Act § 1201(g).