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MEMORANDUM

Re: Schedule M-3/Alternative Disclosure Developments

From: Peter H. Winslow
Samuel A. Mitchell

Date: August 19, 2004

The Department of Treasury recently provided more question-and-answer guidance regarding the new Schedule M-3 and the alternative disclosure procedures in Rev. Proc. 2004-45. In our last mailing, we explained that Rev. Proc. 2004-45 allows corporations to use the new Schedule M-3 as an alternative method of complying with the disclosure requirements for significant book/tax differences described in Treas. Reg. § 1.6011-4(b)(6).

In its most recent guidance, released August 6, 2004, Treasury confirmed that the alternative disclosure methods in Rev. Proc. 2004-45 may be used for tax year 2003, and clarified that partnerships and other business entities may use the alternative disclosure procedure. Among other things, Treasury also clarified that the alternative disclosures on Schedule M-3 should be made on an item-by-item basis rather than on a transaction basis, in spite of the requirements in Treas. Reg. § 1.6011-4(b)(6) and on Form 8886 (the standard form for disclosing significant book/tax differences and other disclosures described in Treas. Reg. § 1.6011(4)(b)), and that only differences greater than \$10 million need be included. Greater than \$10 million items that are included on the angels list in Rev. Proc. 2003-25 need not be included (e.g., life insurance and non-life insurance reserves).

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Treasury also stated that the alternative disclosures under Rev. Proc. 2004-45 must be made on the Schedule M-3 and may not be made on a self-created schedule in lieu of the M-3. This raised the question whether insurance companies can meet the alternative disclosure requirements for 2003 by aggregating differences on Line 30 of Part II of Schedule M-3 and attaching a detailed schedule explaining each item. In its July 7, 2004 guidance, Treasury stated that this aggregation method would be sufficient disclosure on the Schedule M-3 in future tax years for which the Schedule M-3 will be required (2004 and following) for consolidated groups that file on a Form 1120 but have members that file Forms 1120-L or 1120-PC, until specific Schedule M-3 forms tailored for Form 1120-L and 1120-PC returns are released. The IRS Chief Counsel attorney who drafted Rev. Proc. 2004-45 clarified this question for us this week, informing us that insurance groups can meet the alternative disclosure requirements by aggregating the differences and attaching a detailed schedule as described in the July 7, 2004 guidance. The latest guidance prohibiting the use of a schedule in lieu of the Schedule M-3 was intended only to prevent the use of self-created forms. The proper Schedule M-3 is available on the IRS website, at www.irs.gov.

Finally, Treasury also reiterated that the alternative disclosure procedure under Rev. Proc. 2004-45 applies only to the disclosure of significant book/tax differences under Treas. Reg. § 1.6011(4)(b)(6). Other disclosures under Treas. Reg. § 1.6011(4)(b), such as listed transactions, must be made on a Form 8886 pursuant to the requirements in the regulations.

Treasury also addressed a number of other questions (eleven in total). Please call if you have questions.