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House approves permanent small business expensing, S corp incentives

The House of Representatives approved two separate bills that would permanently extend enhanced expensing limits for small businesses and certain incentives benefiting S corporations, all of which expired at the end of 2013.

The America's Small Business Tax Relief Act of 2014 (H.R. 4457), which passed by a vote of 272-144, would make permanent the now-expired enhanced small business expensing limit of $500,000 and phase-out threshold of $2 million under section 179. It also would permanently treat off-the-shelf computer software as qualifying property; permanently treat qualified real property as eligible section 179 property; remove the limitation related to the amount of qualified real property that qualifies as section 179 property; and strike the language in section 179(d)(1) that excludes air conditioning and heating units from the definition of qualifying property.

The Joint Committee on Taxation (JCT) staff estimates the bill would reduce federal revenues by $73 billion over 10 years.

The S Corporation Permanent Tax Relief Act of 2014 (H.R. 4453), which passed by a vote of 263-155, would make permanent the five-year recognition period for built-in-gains tax for S corporations and the basis adjustment for stock of an S corporation making charitable contributions of property at a combined 10-year cost of approximately $2 billion.

No offsets

Neither bill is offset, which proved to be a point of contention for Democratic taxwriters when the legislation cleared the Ways and Means Committee April 29 and again during the floor debate prior to the vote on final passage.

Ways and Means ranking member Sander Levin, D-Mich., and Democratic taxwriter Richard Neal of Massachusetts stated before the final vote they would not support making these business tax extenders permanent but would support a two-year extension.

But Ways and Means Committee Chairman Dave Camp, R-Mich., criticized Democrats for demanding offsets now "despite voting year after year to extend these job-creating policies without being paid for." (In the end, 53 Democrats voted in favor of the permanent enhanced 179 expensing limits and 42 backed the permanent S corporation incentives.)

More in the wings?

Camp noted in a statement released after the vote that the House's action "sends a strong signal to the Senate that permanent tax policy is the right step for businesses to grow and to hire and help hardworking Americans see bigger paychecks. . . . Washington needs to stop its constant tinkering with the tax code and provide permanent tax relief to help strengthen the economy."

The House has now approved three permanent extenders bills since May. (A permanent research credit cleared the chamber on May 9.) Bills that would permanently extend six additional expired tax provisions have cleared the Ways and Means Committee in recent weeks and now await action in the House. These include:

- The subpart F exception for active financing income;
- The lookthrough rule for payments between related controlled foreign corporations;
- Bonus depreciation;
- The deduction for charitable contributions of food inventory;
- The exclusion from gross income for withdrawals from individual retirement accounts by taxpayers over age 70-1/2 for charitable purposes; and
- The increased percentage limits and extended carryforward period for qualified conservation contributions.

(For prior coverage, see *Tax News & Views*, Vol. 15, No. 17, May 2, 2014, and *Tax News & Views*, Vol. 15, No. 21, May 30, 2014.)
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140502_1.html
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140530_1.html

Ways and Means Chairman Camp plans to hold additional hearings and mark-ups on other discrete extenders provisions in the coming months but has not announced which ones might be taken up next. This strategy might be re-examined, however, in the wake of a recent shake-up in the House Republican leadership structure. (See related coverage in this issue.)

White House veto threat

For its part, the Obama administration on June 10 issued two separate statements of administration policy in which it criticized the House approach to extenders and promised that the president would veto the two House-passed bills if they reached his desk in their current form.

Specifically, the administration accused Republicans of "imposing a double standard by adding to the deficit to fund tax breaks for businesses, while insisting on offsetting the cost of measures that help middle-class and working Americans" such as the extension of emergency federal unemployment insurance benefits. "House Republicans also are making clear their priorities by rushing to make business tax cuts permanent without offsets even as the House Republican budget resolution calls for raising taxes on 25 million working families and students by letting important improvements to the Earned Income Tax Credit, Child Tax Credit, and education tax credits expire," the statements said.

Senate developments

The House-approved bills are not expected to be taken up in the Senate, where negotiators are still trying to forge an agreement to move legislation that would retroactively extend through 2015 nearly all of the 55 expired tax extenders at a 10-year cost of $84 billion.

The measure cleared the Finance Committee in early April and was taken up by the full Senate in mid-May; but it was quickly pulled from the floor after Republicans, who were locked in a dispute with Senate Majority Leader Harry Reid, D-Nev., over the process for offering amendments, blocked a procedural motion that would have allowed it to move forward. Finance Committee Chairman Ron Wyden, D-Ore., and ranking Republican Orrin Hatch of Utah have been working without success since then on a plan that would allow for a limited number of amendments. Reid predicted to reporters on June 3 that the chamber is unlikely to approve a final bill until after the midterm congressional elections in November.

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Ripple effects: Cantor's electoral loss and the possible implications for tax policy

House Majority Leader Eric Cantor, R-Va., on June 10 lost his primary bid to serve another term as representative from Virginia's seventh congressional district and informed his GOP colleagues the following day that he would step down from his leadership post by the end of July. Republicans will select their new leader on June 19.

These developments set up a short but intense campaign for Cantor's job – and perhaps others, because if Cantor is replaced by a member currently serving in another leadership position it would create an additional vacancy that would need to be filled. Understanding that the cards have been dealt but only a few have been played thus far, here are some thoughts on what this could mean for tax policy going forward.

Filling the leadership vacancy

Although the field of potential candidates to replace Cantor could still change, at press time current Majority Whip Kevin McCarthy, R-Calif., appears to be uncontested in his bid to move up one rung on the leadership ladder. His path was cleared when several potential candidates opted against running for the post, including House Budget Committee Chairman Paul Ryan, R-Wis., who made clear on June 10 that he will not be a candidate for majority leader or any other party leadership positions that may open up. Ryan's decision to stay out of the leadership race is seen as a clear indication that he instead intends to seek the top spot at the Ways and Means Committee, which will come open in the next Congress when current Chairman Dave Camp, R-Mich., retires at the end of this year. (Note: At press time, Rep. Raul Labrador of Idaho was considering a run for the majority leader job; but he would start his campaign far behind McCarthy.)

Possible implications for tax policy

In the short term, this week's events likely will have little impact on tax policy. We continue to believe that most, if not all, of the now-expired tax extenders provisions will be extended in some form during a lame duck session after the November elections. Ways and Means Chairman Camp has been expected to continue pushing for permanent extension of individual extenders; but that was part of an end-game strategy developed by Majority Leader Cantor, so it may be recalibrated in the coming weeks.

The outlook for the longer term is more uncertain:

- In addition to the short-term shake-up in House leadership, 2015 will bring a new chairman to the Ways and Means Committee. Republicans are favored to retain control of the House, although Cantor's defeat this week reminds us all of the uncertainty of elections. If the GOP does control the House, Paul Ryan and fellow taxwriter Kevin Brady of Texas are the two leading contenders for the post; if control of the House reverts back to the Democrats, the chairmanship would likely be claimed by the current ranking Democrat, Sander Levin of Michigan.
- More in doubt is which party will control the Senate next year. The Republicans would need to net a total of six seats to reclaim the majority and are thought by many nonpartisan observers to be within striking distance of that goal. If that happens, Finance Committee Chairman Ron Wyden, D-Ore., and ranking member Orrin Hatch, R-Utah, are likely to switch places.
- Finally, 2015 will mark the beginning of President Obama's final two years in office. If one or both chambers of Congress are controlled by Republicans, the president will face decisions regarding whether to work with them on achievements to burnish his legacy or whether to instead seek to build his legacy with administrative or regulatory actions rather than through the legislative process.

It is certainly possible to oversimplify and overemphasize the significance of House leadership elections. But there is no doubt that the choices House Republicans make this month will be closely scrutinized for signals as to whether tax reform has a chance to crawl off the mat in 2015 or whether the current tax code will remain law for several more years.

— Jon Traub
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Senators talk of repatriation holiday as offset for highway spending

Talk continued to bubble up in the Senate this week about a temporary repatriation holiday to pay for an upcoming surface transportation infrastructure package, but Finance Committee leaders have yet to indicate that they are on board with the idea.

Highway funding dilemma

Finance Committee Chairman Ron Wyden, D-Ore., has stated that he will hold a mark-up on a highway funding package sometime this month. The current Highway Trust Fund authorization is set to expire September 30, but the fund could run out of money as early as August. (Wyden indicated at a May 6 Finance Committee hearing that the trust fund will require an infusion of approximately $8 billion – on top of amounts projected from existing revenue sources such as taxes on gasoline, diesel fuel, and other transportation-related activities – to remain solvent through the end of the current calendar year.)

Over the longer term, the Senate Environment and Public Works Committee marked up legislation last month that calls for funding surface transportation projects for six years at current levels plus inflation. But the Congressional Budget Office has estimated that keeping the trust fund solvent through 2020 would require another $89 billion beyond what is projected from dedicated revenue sources. If the difference is to be recouped through higher taxes, it will be the Finance Committee's responsibility to develop a proposal to address the anticipated shortfalls.
URL: http://www.cbo.gov/sites/default/files/cbofiles/attachments/45315-TransportationTestimony.pdf

Senate taxwriters have been holding bipartisan meetings to discuss alternatives for replenishing the trust fund and were expected to submit their suggested funding options to Wyden and Finance Committee ranking member Orrin Hatch, R-Utah, over the last few days.

Repatriation, highway spending, & tax reform

The notion of using revenue from a repatriation holiday to bankroll highway spending has already come up in the context of tax reform. The tax reform "framework" released by the Obama administration and the tax reform discussion draft put forward by House Ways and Means Committee Chairman Dave Camp, R-Mich., both include proposals that would dedicate certain one-time revenue from a tax code overhaul to federal infrastructure projects. Camp's discussion draft, which was released in February, relies on a one-time deemed repatriation tax on permanently reinvested offshore income of U.S. multinational firms as part of the transition from a worldwide to a territorial tax regime. President Obama's corporate tax reform framework, released in 2012, relies on revenue that would be generated from the repatriation of certain offshore income as well as various tax timing-related changes such as repealing the LIFO method of accounting and lengthening depreciation schedules.

But some in Congress – notably, Senate Majority Leader Harry Reid, D-Nev., Minority Leader Mitch McConnell, R-Ky., and Sen. Rand Paul, R-Ky. – have either called for or said they would consider a repatriation tax holiday now to address current infrastructure funding needs.

Wyden & Hatch

For their part, Finance Committee Chairman Wyden and ranking member Hatch have been reluctant to embrace the notion of decoupling a repatriation holiday from fundamental tax reform. In a recent joint release announcing upcoming tax reform hearings, the two stated that the Finance Committee will "continue to look for innovative ways to fix the depleted Highway Trust Fund and keep hard-working Americans on the job without diverting revenues from repatriation needed for tax reform."
URL: http://www.finance.senate.gov/newsroom/chairman/release/?id=afb45d67-7bb3-4d0c-bbd7-0c154b930a8d

Since then, however, Wyden has adopted a less adamant public stance, telling reporters that he "has not said yea or nay to any of the options"; but he also has noted anecdotally that certain large multinationals have repatriated substantial amounts this year without the promise of a tax holiday, and in a June 11 print interview he cautioned lawmakers against paying for highway projects with "imaginary savings."

JCT analysis – Hatch appeared to throw cold water on talk of a repatriation holiday on June 9 with the release of a memorandum from Joint Committee on Taxation (JCT) Chief of Staff Thomas Barthold explaining the potential revenue impact of such a proposal. (The JCT staff prepared the memorandum at Hatch's request.)
URL: http://www.hatch.senate.gov/public/_cache/files/1b24c4cf-6005-4a4e-bab7-3d9e3820c509/JCT%206-6-14.pdf

According to the memorandum, reviving Internal Revenue Code section 965 (which was created under the repatriation holiday enacted in the American Jobs Creation Act of 2004) for one year would increase federal revenues by a combined $19.6 billion in 2014 and 2015, but decrease revenues by $115.5 billion from 2016 through 2024, for a net 10-year revenue loss of nearly $96 billion.

The estimate assumes the provision calls for an elective, temporary 85 percent dividends received deduction – amounting to an effective tax rate of 5.25 percent – for certain eligible dividends received by a domestic corporation from controlled foreign corporations. Eligible dividends are those that (1) exceed a specified level of historical average repatriation, (2) do not exceed the greater of $500 million or the amount of overseas earnings identified for financial accounting purposes as permanently reinvested earnings, and (3) are reinvested in the United States pursuant to a dividend reinvestment plan approved by the management and board of directors of the electing corporation and meeting certain other criteria. The estimate assumes that the proposal would be enacted on July 1, 2014, and would permit an election under section 965 for the taxpayer's first taxable year beginning after December 13, 2013.

Barthold explained that the estimate takes into account revenue losses associated with reduced tax liability under section 965 for dividends that taxpayers would have brought back to the United States even without a repatriation holiday, the U.S. tax effects associated with taxpayers changing their dividend repatriation amounts or timing (or both) in response to the proposal, and the potential that some taxpayers might delay planned repatriations within the 10-year budget window if they anticipate that similar repatriation holidays may be enacted in the future.

In a statement released in conjunction with the JCT estimate, Hatch remarked that "[a] tax holiday meant to encourage U.S. companies to repatriate funds from overseas should only be considered when it makes economic sense, such as part of comprehensive tax reform. The Joint Committee on Taxation has clearly outlined the ramifications of a temporary tax holiday, and the outlook is not in the best interest of the American people nor for the coffers of the federal government. It is my hope my fellow lawmakers note these projections when considering options to fund future projects and programs."
URL: http://www.finance.senate.gov/newsroom/ranking/release/?id=d6ced985-e27e-4767-97dc-d9dc75e33ac7

Reid & Paul

Majority Leader Reid and Sen. Paul, however, have suggested that the 2004 provision could be modified so that it would not lose revenue. The two are said to be working together to do just that, although they reportedly are still trying to bridge a gap between Reid's desire for a temporary plan that would impose a 9.5 percent rate on repatriated earnings and Paul's desire for a permanent plan with a 5 percent rate. Paul told reporters on June 11 that the proposal, which is still in the talking stages, "doesn't have absolute parameters" and is "going to take compromise."

Reid and Paul reportedly have discussed their ideas with Wyden and Hatch, and Paul has discussed the proposal with Ways and Means Committee Chairman Camp. But Reid emphasized to reporters on June 10 that "the ultimate decider" on highway funding offsets in the Senate "is going to be Ron Wyden and the Finance Committee."

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Have a question?
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