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Short-term highway funding fix heads to the White House

With the August recess looming, the Senate this week approved and sent to President Obama a House-passed bill intended to replenish the rapidly dwindling Highway Trust Fund and extend its spending authority into 2015. The president is expected to sign the measure into law.

The Highway and Transportation Funding Act of 2014 (H.R. 5021) cleared the Senate by a vote of 81-13 on July 31 – just over two weeks after it was approved in the House by a vote of 367-55. The approved bill would renew Highway Trust Fund spending through May 31, 2015, through an infusion of approximately $10 billion from the general fund and another $1 billion from the Leaking Underground Storage Tank Trust Fund.

The transfer from the general fund would be offset by:

- A so-called "pension smoothing" provision that would modify the interest rate that employers must use to calculate their pension plan liabilities for purposes of determining their annual minimum funding obligations. (The change would generate revenue by lowering an employer's plan funding payments, thereby reducing the value of its deductions for those payments.)
- A provision that would extend Customs user fees for an additional year (through September 30, 2024).

According to estimates from the Joint Committee on Taxation (JCT) staff, the pension smoothing provision would increase federal revenues by approximately $6.4 billion from 2014-2024 and the extension of Customs user fees would increase revenues by roughly $3.5 billion over the same period.
URL: https://www.jct.gov/publications.html?func=startdown&id=4653

Additional details on these provisions are available from the JCT staff.
URL: https://www.jct.gov/publications.html?func=startdown&id=4644

The rocky road to 'yes'

This short-term patch for the Highway Trust Fund heads to the White House after a somewhat complicated journey through the Senate and some additional ping-ponging between the two sides of the Capitol.

Multiple Senate votes – Although the bill as approved by the House on July 15 had the support of the Obama administration, Senate Majority Leader Harry Reid, D-Nev., announced on July 23 that the Senate would hold votes on the House-passed bill and four amendments, including:
URL: http://www.whitehouse.gov/sites/default/files/omb/legislative/sap/113/saphr5021r_20140714.pdf

- A substitute amendment approved by the Senate Finance Committee on July 10 that was similar to the House-passed legislation but included narrower provisions related to pension smoothing and Customs user fees and proposed several taxpayer-compliance offsets that were not in the House bill. (For additional details on the Finance Committee bill, see *Tax News & Views*, Vol. 14, No. 26, July 11, 2014.)
  URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140711_1.html
- An $8 billion substitute amendment from Senate Environment and Public Works Committee Chairman Barbara Boxer, D-Calif., and Finance Committee member Tom Carper, D-Del., that called for extending the Highway Trust Fund's spending authority only through December 19 of this year. (Boxer and Carper argued that that the prospect of the trust fund going broke at year-end would put pressure on Congress to act on a long-term solution in a lame duck session after the November midterm elections.) The amendment included all the Finance Committee offsets except for the pension smoothing provision.
- A proposal from Sen. Mike Lee, R-Utah, that would have, among other things, replenished the Highway Trust Fund through fiscal year 2019 (subject to certain limitations), eliminated the trust fund's mass transit account, phased in a reduction of federal motor fuel taxes, and transferred (on a phased-in basis) greater discretionary authority and fiscal responsibility for surface transportation infrastructure to the states.
- A nontax amendment from Finance Committee member Pat Toomey, R-Pa., that would have eased environmental and permitting requirements for reconstruction of roads, highways, bridges, or transit facilities that are damaged in a natural disaster.

The agreement set a 60-vote threshold for passage of any amendment and of the underlying House bill. (For prior coverage, see *Tax News & Views*, Vol. 15, No. 28, July 25, 2014.)
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140725_2.html

The Senate voted 71-26 on July 29 to replace the language of the House-passed bill with the language approved by the Finance Committee. Later that day, however, it voted 66-31 to strike the Finance Committee language from the now-amended House bill, replace it with the shorter-term Boxer-Carper proposal, and send the revised package back to the House. (The Lee and Toomey amendments failed to meet the 60-vote threshold for passage.)

The House answers back – But the Senate plan faced significant obstacles. Even before the July 29 Senate vote, House Republican leaders had made clear that they would not accept an amended bill, arguing that the tax compliance offsets in the Senate legislation were tantamount to a tax increase and that they would not be forced into hammering out a long-term transportation funding fix during a year-end lame duck session.

With its chances for passage in the House already looking dim, the Senate-amended bill was dealt another blow when the Congressional Budget Office estimated on July 30 that the measure would generate approximately $2 billion less in revenue than the amount needed to offset its proposed $7.1 billion transfer from the general fund to the Highway Trust Fund. In the wake of that development, a spokesman for Speaker John Boehner, R-Ohio, told reporters in a statement July 30 that "the only responsible course is for the Senate to pass the original House-passed highway bill, which we will soon send back to them."
URL: http://www.cbo.gov/sites/default/files/cbofiles/attachments/hr5021.pdf

In a joint statement, Boxer and Carper attributed the revenue shortfall to "a small technical drafting error" that they contended the House could "easily fix." But House leaders on July 31 proceeded with plans to approve a motion to reject the Senate bill – which they did by a vote of 272-150 – and sent the original House-passed language back to the Senate for consideration. Under the twin pressures of a compressed floor schedule and warnings from the Transportation Department

that it was just one day away from cutting payments to states to fund transportation projects, the Senate was left with little choice but to approve the House-passed plan.
URL: http://www.epw.senate.gov/public/index.cfm?FuseAction=Majority.PressReleases&ContentRecord_id=5afb7d7c-c052-d01e-6857-2c892f700dcf&CFID=96854872&CFTOKEN=86189102

Looking ahead

With a short-term fix now in place, lawmakers now face the task of developing a long-term funding proposal by May of next year. House Ways and Means Committee Chairman Dave Camp, R-Mich., told reporters on July 31 that his panel would hold a hearing on the issue in September.

— Victoria Glover
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Corporate insourcing/outsourcing bill stalls in Senate

The Senate on July 29 failed to advance legislation that would provide a 20 percent tax credit for certain expenses related to relocating an offshore business unit to the United States and deny deductions for certain expenses related to eliminating a business unit located within the United States and relocating it offshore. A motion to end debate on the Bring Jobs Back to America Act (S. 2569) was defeated by a margin of 54-42, short of the 60 votes that were required for passage.

The final tally fell almost entirely along party lines: Maine Republican Susan Collins joined 53 Democrats in voting for the motion and Alaska Democrat Mark Begich joined 41 GOP senators in the "no" column.

The outcome was generally expected. Although the Senate had voted 93-7 on July 23 to begin debate on the measure, Republicans closed ranks to keep it from advancing further after Senate Majority Leader Harry Reid, D-Nev., invoked procedural means to prevent them from offering amendments. (A similar partisan disagreement over amendments has blocked progress on several other bills this year, including the tax extenders legislation that cleared the Senate Finance Committee in April.)

The measure was sponsored by Sen. John Walsh, D-Mont., and Finance Committee member Debbie Stabenow, D-Mich. The Joint Committee on Taxation (JCT) staff estimated that it would increase the federal deficit by a net of $214 million over 10 years. (The credit for so-called "insourcing" expenses would result in a revenue loss of $357 million, while the denial of deductions for "outsourcing" expenses would generate $143 million, according to the JCT staff.)
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140801_2suppA.pdf

Stabenow offered similar legislation (S. 3364) in 2012, but it likewise failed to clear a procedural hurdle on the Senate floor. She reintroduced it in 2013. The legislation mirrors a proposal that has been included in previous Obama administration budget packages.

Lew continues push for legislative action on inversions

At the other end of Pennsylvania Avenue, Treasury Secretary Jacob Lew on July 27 reiterated his call for Congress to act swiftly on a near-term fix to address the increase in the number of U.S.-based companies that use mergers with or acquisitions of foreign companies to move their place of residence.

Writing in an op-ed published in *The Washington Post*, Lew acknowledged that "[e]nacting comprehensive tax reform is clearly the best way to address the problems in our tax code that trigger inversions"; but he argued that "[w]hile the business-tax-reform process moves steadily forward, the pace of inversions is increasing at breakneck speed. We must confront this problem now, before our tax base is so eroded as to damage the prospects of comprehensive reform."
URL: http://www.washingtonpost.com/opinions/jacob-lew-close-the-tax-loophole-on-inversions/2014/07/27/2ea50966-141d-11e4-98ee-daea85133bc9_story.html

Lew cited companion bills (H.R. 4679 and S. 2360) introduced in May by House Ways and Means Committee ranking member Sander Levin, D-Mich., and Sen. Carl Levin, D-Mich., respectively, as "strong legislation" that incorporates elements

of the anti-inversion proposals that the Obama administration put forward in its fiscal year 2015 budget proposal. Both versions of the Stop Corporate Inversions Act of 2014 would significantly tighten the rules under section 7874 to provide that an inverted foreign corporation would be treated as domestic for U.S. tax purposes if it meets one of two tests: the first test would be based on continuing ownership of the inverted corporation by legacy shareholders; the second would be based on management and control, without regard to continuing ownership by legacy shareholders of a domestic corporation. (For additional details, see *Tax News & Views*, Vol. 15, No. 20, May 23, 2014.)
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140523_2.html

Lew also contended that, like the two Levin bills, any legislative fix should be retroactive, to avoid "the perverse effect of encouraging corporations to act more quickly, negotiate new deals, and rush to close those transactions before the bill is enacted. (The Levin bills would be effective for transactions on or after May 8, 2014.)

Lew made a similar case in a July 15 letter he sent to the chairmen and ranking members of the two congressional taxwriting committees. (For prior coverage, see *Tax News & Views*, Vol. 15, No. 27, July 18, 2014.)
URL: http://www.hatch.senate.gov/public/_cache/files/b6800ed3-979e-4edd-a832-8a1b6475b624/7-15-2014%20Final%20Hatch%20Letter.pdf
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140718_1.html

Former Treasury official calls for regulatory fix

Lew's remarks were published just one day after former Treasury Deputy Assistant Secretary for International Tax Affairs Stephen Shay argued in an opinion piece published in Tax Notes that the Treasury Department can – and should – use regulatory authority to curb inversion transactions.
URL: http://www.taxanalysts.com/www/features.nsf/Features/76D1FDB318A0435D85257D230050CC38?OpenDocument

According to Shay, the explicit language of section 385 gives Treasury the authority to issue regulations that would reclassify related-party debt as equity and convert interest deductions into nondeductible dividends. Such a move would not prevent cross-border combinations "that are grounded on real business objectives" but it "would materially reduce the incentive for a U.S. corporation to expatriate for tax-motivated reasons," Shay wrote.

Regulatory action also would stop the pace of inversions and give Congress time to "work toward real international tax reform," Shay noted.

House, Senate bills would deny federal contracts for inverted entities

In other developments, Rep. Rosa DeLauro, D-Conn., Rep. Lloyd Doggett, D-Tex., Sen. Dick Durbin, D-Ill., and Sen. Carl Levin introduced companion bills in the House and Senate this week that generally would prohibit the award of federal government contracts to inverted domestic corporations and certain joint ventures.

The No Federal Contracts for Corporate Deserters Act (H.R. 5278 and S. 2704) would define an inverted company based on the continuing ownership and management-and-control tests provided in the broader Stop Corporate Inversions Act that the Levin brothers introduced in the House and Senate.
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140801_2suppB.pdf

The Levin brothers' bill would be effective for inversion transactions after May 8, 2014. The effective date in the contracting prohibition in the No Federal Contract for Corporate Deserters Act is more sweeping, however, and would apply to companies that invert "before, on, or after May 8, 2014."

Schumer to unveil earnings-stripping proposal in August

For his part, Senate Finance Committee member Charles Schumer, D-N.Y., told reporters July 31 that he intends to unveil legislation during the August recess intended to curb inversion transactions by tightening the earnings-stripping rules under section 163(j). Although he provided no details, Schumer said his plan "tends to have some Republican support" and that it could be compatible with the House and Senate anti-inversion bills sponsored by the Levin brothers.

— Jon Almeras & Michael DeHoff
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Camp promises bipartisan offsets for ABLE Act

House Ways and Means Committee Chairman Dave Camp, R-Mich., said July 31 that he was committed to finding bipartisan offsets to pay for legislation that would create tax-preferred savings accounts that would allow individuals with disabilities and their caregivers to pay for certain qualified disability expenses.

The Achieving a Better Life Experience (ABLE) Act of 2014 (H.R. 647), which cleared the Ways and Means Committee by voice vote at a July 31 mark-up, would allow eligible individuals to establish and contribute to "qualified ABLE accounts" under a "qualified ABLE program." Qualified ABLE accounts and qualified ABLE programs would be treated for income tax purposes in the same manner as accounts in a qualified tuition program under section 529. Contributions to an ABLE account would not be deductible but earnings would accumulate on a tax-deferred basis. Funds in the accounts could be used to pay for "qualified disability expenses" for education (including higher education), a primary residence, transportation, obtaining and maintaining employment, health and wellness, and other personal support expenses. Additional details on the legislation are available in a description prepared by the Joint Committee on Taxation (JCT) staff.
URL: https://www.jct.gov/publications.html?func=startdown&id=4660

The measure as approved does not include revenue offsets and the JCT staff estimates it would increase the deficit by just over $2 billion from 2015-2024. But in his opening statement at the mark-up, Camp noted that he and Ways and Means ranking Democrat Sander Levin of Michigan had agreed "to find bipartisan pay-fors" that could "easily pass the House and Senate." Camp added that Ways and Means Committee staff would immediately "begin serious discussions on how we pay for this bill."
URL: https://www.jct.gov/publications.html?func=startdown&id=4662

The ABLE Act was introduced in 2013 by Rep. Ander Crenshaw, R-Fla., and has 379 House co-sponsors. A Senate companion bill (S. 313) introduced last year by taxwriter Robert Casey, D-Pa., awaits action in the Finance Committee. That bill has 74 co-sponsors.

— Michael DeHoff
Tax Policy Group
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Ways and Means panel looks at dynamic score of tax reform

Several economists speaking at a July 30 House Ways and Means Select Revenue Measures Subcommittee hearing recommended that congressional scorekeepers employ dynamic analysis to help taxwriters judge the best policies to encourage economic growth and defended its use in estimating the effects of the tax reform discussion draft that Ways and Means Committee Chairman Dave Camp, R-Mich., unveiled earlier this year.

Camp's tax reform discussion draft, which he released in February, was accompanied by two revenue estimates from the Joint Committee on Taxation (JCT) staff. The first was a traditional "static" score, which showed that the proposal would not increase the deficit over 10 years. The second was a so-called "dynamic" score, which includes estimates about the macroeconomic impact of the proposal. It projected that Camp's plan would boost the size of the economy overall and therefore also boost federal receipts by between $50 billion and $700 billion over 10 years, depending on which assumptions and models are used to make the calculations. (For coverage, see *Tax News & Views*, Vol. 15, No. 9, Feb. 27, 2014).
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140227_1.html

Republicans on the subcommittee, including Chairman Pat Tiberi, R-Ohio, were supportive of the use of dynamic scoring to estimate the impact of comprehensive tax reform. Democrats, however, were not as enthused. Subcommittee ranking member Richard Neal, D-Mass., stated that he "was not categorically opposed" to dynamic scoring but cautioned against over-reliance on that revenue-estimating technique as a way to justify large tax cuts.

Supporters

Most of the witnesses at the hearing defended the use of dynamic scoring and its ability to better gauge the effects of tax reform.

For example, Scott Hodge of the Tax Foundation said economic growth should be the primary objective of tax reform, and for this reason, dynamic analysis was an essential tool in determining the best policy. Curtis Dubay of the Heritage Foundation noted that the inclusion of a dynamic score was a "long overdue and welcome change to how tax policy is discussed at the federal level."

Douglas Holtz-Eakin, former director of the Congressional Budget Office and now with the American Action Forum, explained that so-called "static" scoring assumes there is a fixed outlook for the overall economy. He said that static scoring does take some incentive effects into account but it assumes no effect on the macro economy. Because this fails to account for broader economy-wide impacts of major policy changes, he contended that tax reform proposals should be dynamically scored. This would give policymakers the ability to judge proposals that have the same budget cost using traditional metrics but differ in their overall economic impact, he said.

Holtz-Eakin said the basic mission of scoring is to "rank competing proposals in a systematic fashion so policymakers can identify which proposals are better or worse from a growth and budget perspective." In later questioning from Neal, Holtz-Eakin reminded the subcommittee that the models were just that – "models, not reality" – and should not be used to say that something will certainly happen. Dubay expressed a similar view. "It's better to be approximately correct than precisely wrong," he said.

Hodge also urged the JCT to make its scoring process more transparent. "Show us your work," he said, explaining that although the JCT provides general descriptions of their models and basic parameters, it gives little information about its assumptions inside and outside the model and how specific results are achieved. He told the subcommittee that transparency would help the JCT refine and improve its analysis. In his written testimony, Hodge included a list of specific questions he thinks the JCT should answer to make the process less opaque.

And critics

John Buckley, a former chief tax counsel for the Ways and Means Committee and former JCT chief of staff, was critical of dynamic scoring, saying the models and their underlying assumptions were divorced from reality. Buckley said the models were based on supply-side economic theories that are no longer "relevant in a world where companies, responding to market forces, are moving production offshore where there is a virtually unlimited supply of labor."

Buckley also used the hearing to criticize Chairman Camp's tax reform discussion draft, saying the proposal would increase the cost of capital for domestic companies and therefore would reduce domestic business capital. The Camp draft would largely benefit "existing corporate investments, whereas the 'business reforms' in the Camp proposal [would] largely reduce incentives for future investments," he said.

Buckley cited economic research that shows that almost all employment growth in the United States between 1990 and 2008 occurred in the "non-tradable" sector – that is, industries not subject to cross-border competition, such as government, health care, and retail. Camp's plan, he argued, would only exacerbate the problem: it would not create an "even playing field"; rather, it would tilt U.S. tax policy toward encouraging foreign over domestic investment, he said. Buckley emphasized this point in questioning from subcommittee member John Larson, D-Conn., saying that the Camp draft would place a heavy burden on capital investment in domestic manufacturing.

In his written testimony, Buckley delved further into a critique of macroeconomic models based on supply-side principles. For example, he said that the models assumed full employment and no unused business capital and therefore project immediate economic growth from a larger labor supply even when there is substantial existing unemployment. He was also critical of the assumption of individual reaction to incentives. Buckley said the JCT model assumes that individuals act on the basis of current conditions without the ability to accurately predict the future. The dynamic models often assume "perfect foresight," he said.

Tiberi asked the other witnesses about this, and Diamond replied that perfect foresight is a good average of the various ways individuals will respond. Buckley had also criticized Diamond's model for assuming a fix of the nation's long-term debt problem, but Diamond responded that a fix had to be assumed whether it was tax increases, reduced spending, or some combination of both. If the fix to our deficit problem is higher tax rates, then the positive macroeconomic effect of subsequent tax reform that lowers those rates is even larger, he said.

Written testimony available

Written testimony that was submitted for the hearing is available on the Ways and Means Committee Web site.
URL: http://waysandmeans.house.gov/calendar/eventsingle.aspx?EventID=388945

— Jon Almeras
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Deloitte Tax LLP

Bill would mandate disclosure of tax treatment of settlements between taxpayers and federal agencies

The Senate Homeland Security and Governmental Affairs Committee on July 30 approved bipartisan legislation that would, among other provisions, require public disclosure of information regarding the tax treatment of nonconfidential settlement agreements reached between taxpayers and federal agencies that involve more than $1 million in payments.

Nonconfidential settlements

The Truth in Settlements Act of 2014 (S. 1898), which is sponsored by Sens. Elizabeth Warren, D-Mass., and Tom Coburn, R-Okla., was approved by voice vote. Notable tax-related provisions applicable to nonconfidential settlements would:

- Require federal agencies to explain in written public statements that refer to a settlement amount whether any portion of that amount is classified as restitution or compensation (which generally is tax deductible) or as a penalty or fine (which is not deductible).
- Require federal agencies to post on their Web sites basic information about settlement agreements – including their classification as deductible restitution or compensation or nondeductible penalties or fines. Agencies also would be required to post copies of the settlement agreements.
- Require companies that settle with enforcement agencies to state in their filings with the Securities and Exchange Commission whether they have deducted any settlement payments from their taxes.

Confidential settlements

In the case of confidential settlements, the legislation would require federal agencies to explain why an agreement was deemed confidential and to submit an annual report to Congress providing aggregate statistics on their confidential settlement agreements. It also would direct the Government Accountability Office to examine how, and to what extent, agencies deem settlements confidential, and whether there are ways to make that process more transparent.

Next steps

The legislation has been referred to the full Senate, although it is unclear when (or whether) Majority Leader Harry Reid, D-Nev., intends to bring it to the floor. An identical companion bill (H.R. 4324) was introduced in the House on March 27 by Rep. Matt Cartwright, D-Pa. It was referred to the House Financial Services Committee and the Committee on Oversight and Government Reform but has not been taken up by either panel.

— Michael DeHoff
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Lawmakers hint at post-recess agenda

As Congress prepared to leave Washington for a five-week district work period, House and Senate leaders this week offered hints on some of the tax issues that could see floor action when the legislative session resumes on September 8.

House

House Ways and Means Committee Chairman Dave Camp, R-Mich., told reporters July 30 that the chamber could vote on legislation to repeal the estate tax, although he noted that no final decisions had been made. An estate tax repeal bill (H.R. 2429) introduced by Ways and Means Committee member Kevin Brady, R-Texas, has 221 co-sponsors.

Camp did not indicate whether he expected the House to take up legislation approved in the Ways and Means Committee in May that would permanently extend the exception under subpart F for active financing income and the lookthrough rule for payments between related controlled foreign corporations, but he did suggest that House taxwriters could mark up additional permanent extenders provision in the next work period.

Senate

Across the Capitol, Senate Majority Leader Harry Reid, D-Nev., told reporters on July 31 that lawmakers in his chamber would take up a short-term extension of the Internet Tax Freedom Act (ITFA) during their first two weeks back from the summer recess.

The ITFA, which is set to expire November 1, imposes a moratorium on state and local Internet access taxes and provides protections for Internet access taxes that were levied in certain states before October 1998 and grandfathered into the moratorium. Senate Finance Committee Chairman Ron Wyden, D-Ore., urged his colleagues to take up a temporary ITFA extension during a July 31 floor statement. Although he has drafted legislation that would make the moratorium permanent, Wyden indicated that a permanent extension is "not a political reality" and that another temporary extension could serve as a "bridge" to a permanent fix. (The House passed legislation on July 15 that would permanently extend the moratorium on taxes on electronic commerce but that would allow the grandfathering provisions to expire. For prior coverage, see *Tax News & Views*, Vol. 15, No. 27, July 18, 2014.)
URL: http://www.finance.senate.gov/newsroom/chairman/release/?id=86bf938b-5c36-49ec-a0b7-cda199a63b30
URL: http://newsletters.usdbriefs.com/2014/Tax/TNV/140718_4.html

Wyden added that he hopes to keep the debate over the ITFA separate from discussions about the Marketplace Fairness Act – legislation he opposes – which would make it easier for a state to capture sales and use tax revenue from transactions involving online and other "remote" vendors that do not have an in-state physical presence. Finance Committee member Mike Enzi, R-Ohio, and Senate Majority Whip Richard Durbin, D-Ill., among others, recently introduced legislation that would couple a 10-year extension (through November 1, 2024) of the ITFA with provisions from the Marketplace Fairness Act. But Wyden argued that the Senate "can move this short-term extension [of the ITFA] today while we work out the issues raised by those who believe that allowing localities to collect taxes across the country is more important than a ban on discriminatory taxation."

Tight timeline

Lawmakers are expected to remain in Washington for only a brief period after the recess before they adjourn to make a final campaign push in advance of the midterm congressional elections. The House is currently set to be in session for 12 days (September 8-11, September 16-19, and September 29-October 2.) Majority Leader Reid has indicated that he hopes that the Senate will wrap up its pre-election work by September 23 and that he may keep the chamber in session on weekends to adhere to that schedule.

— Michael DeHoff
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A note on our publication schedule

At press time, the House remained in session past its scheduled adjournment date as it wrestles with a border security bill. Once action on that measure is completed, Congress is expected to be out of session through September 5 as lawmakers leave Washington for the summer district work period. Nevertheless, developments on important tax issues may continue behind the scenes. *Tax News & Views* will publish during the recess whenever events warrant.

— Jon Traub
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Have a question?
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