Tax

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Rumors swirl, but path forward for extenders remains unclear

Talk of a possible extenders deal that would make some expired tax provisions permanent and revive others for at least two more years swirled through Washington during the congressional Thanksgiving recess and into the current post-recess work week. But as of press time, longstanding obstacles continue to block the path to a final agreement.

The rumored goal

Reports emerged during the week of November 23 that congressional taxwriters and staff were working to put together the framework for an agreement that would incorporate many of the Republican-backed permanent tax extenders that have already been approved either on House floor or in the Ways and Means Committee – for example, the research and experimentation credit, bonus depreciation, increased expensing limits under section 179, the deduction for state and local general sales taxes, and charitable giving incentives. (In recent years, House Republicans have pushed for permanent extensions of selected temporary tax provisions as a way to make tax reform easier for a future Congress by building those measures into the budget baseline and lowering revenue targets, which in turn would give taxwriters more flexibility as they decide what base broadeners may be necessary to reach a desired level of rate reduction.)

Congressional Democrats have a wish list of their own – namely, permanent extensions of the American Opportunity Tax Credit and enhancements to the earned income tax credit (EITC) and the child tax credit (CTC), all of which are scheduled to expire in 2017. Democrats are also said to be pushing for a provision that would index the CTC to inflation. But in exchange for any expansion of the EITC and CTC, Republicans are demanding the addition of provisions to guard against fraud and abuse in those programs.

If negotiators reach an agreement to make some provisions permanent, it is expected that remaining extenders would be extended retroactively, but it is unclear whether that would be for two years (as proposed in legislation approved by the Senate Finance Committee in July) or for a longer period.

Obstacles

But with the recess over and Congress now back in session, it appears that lawmakers remain divided over the potential cost of a permanent extenders package and concerns over policy issues related to the earned income and child tax credits.

Cost concerns: Unofficial estimates indicate that an expansive extenders package could increase the deficit by between $700 billion and $800 billion over 10 years. That cost could go even higher if other items – such as repeal or delay of the “Cadillac” tax on high-cost health insurance policies or the medical device excise tax, which were enacted as part of the Patient Protection and Affordable Care Act of 2010 – are added into the mix. Thus far, revenue offsets to defray some of the cost of an extenders package have not been part of the negotiations.

Some lawmakers could be reluctant to support a high-cost extenders bill. Senate Finance Committee Chairman Orrin Hatch, R-Utah, for example, cautioned in remarks to reporters this week that the extenders package “could get too big where it won’t pass at all.”

“Everybody has to look at it and say ‘let’s do the art of the doable,” Hatch said.

House Ways and Means Committee member Pat Tiberi, R-Ohio, on the other hand, told reporters this week that policy should be the primary focus of the extenders debate.

“The contents are more important than the cost,” he said.

CTC, EITC safeguards: Congressional Democrats and the Obama administration have stated that they will not agree to permanent extensions of business tax incentives without permanent extensions of enhancements to the child tax credit and earned income credit that were enacted in the 2009 stimulus bill. But Republicans have been wary of extending the EITC and CTC enhancements, mainly due to concerns about high error rates and perceived fraud, and have stated that the only acceptable tradeoff for their inclusion in this year’s extenders bill is the addition of new anti-abuse provisions.

In a December 2 news release, the Republican Study Committee, a caucus of about 170 conservative House members, argued against renewing “stimulus legacy items like the expanded Earned Income Tax Credit…and the additional Child Tax Credit...without making significant improvements to the programs’ verification and oversight.”

It remains unclear, however, whether lawmakers can unlock a permanent extenders deal by crafting measures that improve compliance and reduce fraud in those programs in a way that addresses GOP concerns but does not cause Democrats to feel that the essential anti-poverty features of those credits are being undermined.

Outlook

Although the shape of a final deal remains uncertain, most observers continue to believe the tax extenders will be dealt with in some fashion before the end of the year, possibly in conjunction with appropriations legislation which must be enacted by December 12 in order to avoid a partial government shutdown. (Depending on the progress of the appropriations bill, lawmakers could extend their deadline into the week of December 14 by approving a short-term continuing resolution to keep the government funded. Both chambers are currently scheduled to adjourn for the year on December 18.)

House Ways and Means Committee Chairman Kevin Brady, R-Texas, told reporters December 2 that negotiators have made “a lot of progress” and that a large extenders deal is “very much doable,” although he acknowledged that “in the end, it may not go all the way through.”

If efforts to reach a permanent extenders deal fall flat, lawmakers likely will opt instead for a temporary package. But that scenario, Finance Committee Chairman Hatch told Bloomberg BNA December 2, would necessitate a multi-year deal in order to avoid a repeat of last year’s extenders process, in which already-expired provisions were renewed retroactively for one year late in December, only to expire again a mere two weeks later.

“We’re not going to put up with one year,” he said.

— Michael DeHoff
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Five-year highway bill – with tax compliance provisions – heads to White House

Congress this week approved and sent to President Obama a five-year, $305 billion infrastructure spending package that includes some tax compliance provisions but relies primarily on nontax offsets to provide an infusion of new revenue for the cash-strapped Highway Trust Fund. The Fixing America’s Surface Transportation (FAST) Act (H.R. 22) cleared the House and Senate on December 3, just one day before the scheduled expiration of the latest short-term patch for Highway Trust Fund spending authority. President Obama is expected to quickly sign the measure into law.

Passage of the FAST Act marks the first time since 2005 that Congress has sent a long-term transportation bill to the White House.

No increase in dedicated Highway Trust Fund excise taxes

The FAST Act would extend spending authority for the Highway Trust Fund through September 30, 2020. The fuel and nonfuel excise taxes that provide the dedicated revenue stream for the Highway Trust Fund generally would be extended at their current levels through September 30, 2022. The heavy vehicle use tax would be extended at its current level through September 30, 2023. (As the debate over a long-term highway bill unfolded in recent months, there were calls in some circles for Congress to stick to a "user-pays" approach to funding infrastructure spending; but a hike in transportation-related excise taxes – particularly those imposed on gasoline and diesel fuel – proved to be politically unpopular and did not receive a vote in the House or the Senate.)

New revenue provisions

To close the gap between projected Highway Trust Fund revenue and anticipated spending levels – a shortfall the Congressional Budget Office has estimated to amount to about $16 billion a year – the FAST Act relies primarily on nontax provisions that call for, among other things, selling some of the oil from the Strategic Petroleum Reserve, reducing the amount of interest that the Federal Reserve pays to certain member banks, and shifting funds from a Federal Reserve surplus account.

On the tax side, the FAST Act includes two compliance provisions that would:

- Require the Internal Revenue Service to use private debt collection agencies to recover certain unpaid tax debts that are owed to the government but are not actively being pursued by the IRS for collection, effective for tax receivables identified after the date of enactment. According to a summary of the FAST Act conference agreement, the provision would *not* apply to receivables that (1) are subject to a pending or active offer in compromise; (2) are the subject of an innocent spouse case; (3) involve taxpayers who are deceased, under the age of 18, serving in a designated combat zone, or victims of identity theft; (4) are currently under examination, litigation, criminal investigation, or levy; or (5) are subject to a proper exercise of a right to appeal. The Joint Committee on Taxation (JCT) staff has estimated that the provision would increase federal receipts by $2.4 billion between 2016 and 2025.
  URL: https://www.jct.gov/publications.html?func=startdown&id=4854
- Permit the State Department to deny new passports to and revoke existing passports held by certain taxpayers who have more than $50,000 in delinquent tax debts, effective upon enactment. The conference agreement summary notes that the provision includes a number of taxpayer safeguards, such as notification requirements and a mechanism allowing the IRS to correct errors and take into account a taxpayer's actions to come into compliance. According to the JCT, this provision would increase federal receipts by an estimated $395 million over 10 years.

The FAST Act also would repeal a provision in the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 (P.L. 114-41, a short-term highway funding patch that was enacted on July 31) that gives certain employee benefit plans an automatic three-and-a-half month extension for filing a Form 5500. (The three-and-a-half month extension applies to returns for taxable years beginning after December 31, 2015.) Under the

FAST Act, the extension period would revert to two-and-a-half months from the Form 5500's due date, as in effect under Department of Labor and Internal Revenue Service rules before the enactment of P.L. 114-41. The JCT has estimated that this provision will have a negligible revenue effect.

Hatch: FAST Act a 'watershed moment'

In remarks on the Senate floor December 1, Finance Committee Chairman Orrin Hatch, R-Utah, characterized the FAST Act conference agreement as "a watershed moment for our transportation community."

"We've heard time and again that a long-term highway bill would only be possible if we included a big tax increase. Yet we've been able to defy the odds and provide much-needed funding for America's bridges, highways, and roads for the next five years," Hatch said.

CBO projects long-term highway revenue shortfall

For its part, however, the nonpartisan Congressional Budget Office (CBO) indicated in a revenue estimate released December 2 that while the Fast Act addresses the Highway Trust Fund's near-term revenue needs, the trust fund nonetheless faces a revenue shortfall over the longer term.
URL: https://www.cbo.gov/publication/51051

According to CBO, Highway Trust Fund spending under the FAST Act would total $280 billion between 2016 and 2020, revenues and interest credits would total $208 billion, and transfers from Treasury's general fund would total $70 billion. At the end of fiscal year 2020, however, CBO projects a balance of only $8 billion in the trust fund's highway account and $2 billion in its transit account. And beginning in fiscal year 2021, revenues credited to the highway and transit accounts "would be insufficient to meet the trust fund's obligations."

House Transportation and Infrastructure Committee Chairman Bill Shuster, R-Pa., told reporters December 3 that it was up to lawmakers and stakeholders to address the Highway Trust Fund's revenue needs over the long term.

"Everybody's got to be on the same page, and then we have to go out and sell it to the American people and sell it to the legislators," he said.

— Michael DeHoff
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International Tax Alert: Treasury releases new anti-inversion guidance

The Treasury Department on November 19 released Notice 2015-79, which announces its intent to issue regulations that would tighten the anti-inversion rules of Internal Revenue Code section 7874 and reduce the tax benefits of inversion transactions.
URL: http://newsletters.usdbriefs.com/2015/Tax/TNV/151204_3suppA.pdf

Details on the new guidance are available in this alert from Deloitte LLP's International Tax Group.
URL: http://newsletters.usdbriefs.com/2015/Tax/TNV/151204_3suppB.pdf

— Michael DeHoff
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Senate OKs repeal of medical device, 'Cadillac' taxes under budget fast-track process

The Senate voted 52-47 on December 3 to approve an amended version of House-passed legislation that would, among other things, repeal two controversial excise taxes and defang the health insurance coverage mandates for individuals and employers enacted in the Patient Protection and Affordable Care Act of 2010 (PPACA).

The Restoring Americans' Healthcare Freedom Reconciliation Act of 2015 (H.R. 3762) cleared the Senate under the fast-track budget reconciliation process, which allows for passage of certain legislation in that chamber by a simple majority vote, as opposed to the 60 votes normally required to clear procedural hurdles – a useful tool for Senate Republicans, who currently hold 54 seats.

Although the House has voted multiple times in recent years to repeal the PPACA in its entirety or in discrete parts, Senate passage of H.R. 3762 marks the first time a PPACA repeal measure has been able to clear both chambers. But that milestone is largely symbolic: assuming the House and Senate are able to reconcile the differences in their respective versions of the legislation, H.R. 3762 will head to the White House only to face a certain veto from President Obama.

Excise taxes, insurance mandates

Like the House version of H.R. 3762 that was approved in October, the Senate-approved measure would eliminate:

- The 2.3 percent excise tax imposed on the sale of certain medical devices, which became effective for sales of such devices after December 31, 2012, and
- The 40 percent excise tax imposed on certain high cost employer-sponsored health coverage (known as the "Cadillac" tax), which is scheduled to take effect in 2018, as well as the current requirement that employers annually report the cost of each employee's employer-sponsored health coverage on their Form W-2. Although the Senate substitute to the House-passed version of H.R. 3762 originally called for delaying implementation of the Cadillac tax until 2025, lawmakers approved an amendment during floor debate that would repeal the tax outright.

The medical device and Cadillac taxes have come under fire from Republicans and Democrats alike in both chambers, although Democrats generally have conditioned their support for

repealing these provisions upon identifying offsetting revenue. Finding offsets, however, poses a steep challenge given estimates from the JCT that repealing the Medical device and Cadillac taxes would reduce federal revenues by $23.9 billion and $91.1 billion, respectively, over the next 10 years.
URL: https://www.jct.gov/publications.html?func=startdown&id=4838

The House version of the measure also would repeal the PPACA's insurance coverage requirements under the individual and employer mandates. To avoid potential parliamentary concerns, Senate managers modified their bill to retain the two mandates but reduce the penalties for noncompliance to zero.

The Senate bill includes a provision not in the House version that would modify the rules related to recapture of excess advance payments of health insurance premium tax credits to eligible low-income individuals. It also includes certain nontax changes that were added to win support of certain Senate Republicans who were concerned that the measure did not go far enough in repealing the PPACA.

Tax provisions part of a broader reconciliation package

House and Senate Republicans moved their respective versions of H.R. 3762 pursuant to the budget reconciliation instructions that were included in the fiscal year 2016 budget resolution adopted by Congress earlier this year. The budget resolution requires three House panels (the Ways and Means Committee, the Energy and Commerce Committee, and the Committee on Education and the Workforce) and two Senate committees (the Finance Committee and the Health, Education, Labor, and Pensions Committee) – all of which have jurisdiction over various policies included in the PPACA – to each report legislation that on net reduces the deficit by $1 billion over 10 years.

In addition to the tax-related provisions from the Finance Committee, the Senate-approved bill incorporates separate reconciliation measures reported out of the Health, Education, Labor, and Pensions Committee that would repeal certain nontax elements of the PPACA.

Other tax amendments

The Senate also considered a number of tax provisions during a marathon session of amendment votes known as the "vote-a-rama." In addition to the amendment to repeal the Cadillac tax, the chamber approved a GOP-sponsored sponsored provision that would extend through 2021 the 7.5 percent adjusted gross income floor for individuals age 65 and over who wish to claim the itemized deduction for medical expenses. (The current-law provision is set to expire at the end of 2016.)

The Senate rejected a string of proposed Democratic amendments with provisions that called for tightening anti-inversion rules, imposing a Fair Share tax on certain upper-income individuals, treating carried interest income as ordinary, and repealing the performance-based compensation and commission exceptions under section 162(m) related to nondeductible employee remuneration.

Although the underlying legislation is not expected to become law, the amendments adopted (and rejected) in the vote-a-rama highlight lawmakers' legislative priorities and are often more noteworthy for their later use in campaign commercials than for their impact on the legislative process. At the same time, amendments that are approved with significant bipartisan support can often provide momentum for subsequent legislative efforts.

Obama promises veto

As expected, President Obama has promised to veto the Senate-approved bill.

"By repealing numerous, key elements of current law, this legislation would take away critical benefits and health care coverage from hard-working middle-class families," the White House said in a December 2 statement of administration policy. "Rather than refighting old political battles by once again voting to repeal basic protections that provide security for the middle class, members of the Congress should be working together to grow the economy, strengthen middle-class families, and create new jobs," the statement said.
URL: https://www.whitehouse.gov/sites/default/files/omb/legislative/sap/114/saphr3762s_20151202.pdf

The president has issued similar veto threats against the House-passed reconciliation bill as well as the other PPACA repeal measures approved in that chamber in recent years.

Republicans would not seem to be in a position to corral the two-thirds majority in the House and Senate that would be required for a veto override.

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Ryan identifies tax reform as key part of economic agenda

House Speaker Paul Ryan, R-Wis., used a December 3 policy address to call for a tax code overhaul as part of a "pro-growth" economic agenda aimed at "creating jobs and raising wages."
URL: https://www.youtube.com/watch?v=HytBikkoTyc&feature=youtu.be

In a speech delivered at the Library of Congress in Washington, Ryan advocated lowering the corporate tax rate to allow US businesses to be competitive overseas, reducing the rate for domestic small businesses, collapsing the current seven individual marginal rate brackets to "two or three," and simplifying the code by eliminating certain unspecified tax "loopholes" and using the resulting savings "to cut tax rates for everybody."

Ryan acknowledged that repealing some current-law tax provisions in order to bankroll a reduction in rates could prove unpopular among certain constituencies; but he argued that simplification would result in "a tax code that rewards good work instead of good connections," which, in turn, would spur economic growth.

“When people know they will keep more of their hard-earned money, they will work more, save more, invest more – and create more jobs for all of us. And when there is more work to go around, more people will see their wages go up,” he explained.

In a press release issued shortly after Ryan’s remarks, Ways and Means Chairman Kevin Brady, R-Texas, reiterated his intention to “marshal the resources and ideas of the House to create a fairer, flatter, and simpler tax code that is built for growth.”

GOP tax reform bill in 2016?

Ryan has been a vocal advocate for tax reform dating back to his days as chairman of the House Budget Committee and his recent, albeit brief, tenure as chairman of the Ways and Means Committee. (He became Ways and Means chairman when the 114th Congress convened in January but left the panel when he was elected House speaker at the end of October.)

Because of longstanding policy differences between the White House and congressional Republicans on key individual income tax issues – notably, whether tax reform should be used to raise revenue and make the tax code more progressive – comprehensive tax reform is now considered unlikely until after the Obama administration is out of office. But in remarks last month at an event hosted by *The Wall Street Journal*, Ryan stated that House Republicans may attempt to pass tax reform in 2016 – before the November congressional and presidential elections – as a way to help draw a contrast with Democrats and to demonstrate the direction a Republican-led Congress and White House would take on US tax policy.

BEPS recommendations highlight need for international reform

Ryan also indicated at last month’s *Wall Street Journal* event that he continues to work with Senate Finance Committee members Rob Portman, R-Ohio, and Charles Schumer, D-N.Y., on an international reform plan that would transition the US toward a territorial system for taxing foreign-source income of domestic multinationals, implement an “innovation box” for income from certain intellectual property, put in place certain measures to prevent erosion of the US tax base, and impose a “deemed repatriation” tax on US firms’ untaxed foreign profits. (Ryan had hoped to include an international reform package as part of a long-term highway spending bill this fall, but that plan stalled after he and Schumer were unable to agree on an appropriate level of highway funding.)

The issue of international tax reform has come into the spotlight with the recent release of the OECD’s final report on its Base Erosion and Profit Shifting (BEPS) project, which recommends, among other things, the implementation of nexus-related limitations on patent box regimes – a recommendation that some in Congress fear could create incentives for US businesses to redirect their research and development spending and other activities overseas to take advantage of other countries’ regimes.

Lawmakers contended at separate hearings held by the Ways and Means Tax Policy Subcommittee and the Senate Finance Committee on December 1 that the BEPS project serves as a compelling reason for Congress to address corporate, and especially international, tax reform.

Tax Policy Subcommittee Chairman Charles Boustany, R-La., cautioned that “[w]e are out of time” and called on Congress to take “the tough but necessary steps to reform our tax code.”

Finance Committee ranking Democrat Ron Wyden of Oregon told colleagues on his panel that “if you’re a member of Congress with concerns about BEPS, …then comprehensive tax reform is your opportunity to design the tax system our nation needs. …If you want to give companies a reason to invest, grow, and headquarter in the US, comprehensive tax reform is the only path to reach those goals.”

Witness testimony presented at the hearings is available on the Ways and Means and Finance Committee websites.
URL: http://waysandmeans.house.gov/event/chairman-boustany-announces-hearing-on-the-oecd-base-erosion-and-profit-shifting-beps-project/
URL: http://www.finance.senate.gov/hearings/hearing/?id=4caf79c9-5056-a055-6448-a1665d204f15

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