CCH Tax Briefing

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Fiscal Year (FY) 2014 Budget Proposals

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Special Report

HIGHLIGHTS

- New "Fair Share Tax" On Higher Income Taxpayers
- Limit on Accrual of Retirement Benefits
- Return Estate Tax To 2009 Parameters
- 10 Percent Tax Credit For New Hires/Increased Payrolls
- Permanent Research Tax Credit
- House And Senate FY 2014 Budgets
- House And Senate Working Groups On Tax Reform

INSIDE

White House, GOP Look For Common Ground In Dueling Proposals On Tax Reform/Deficit Reduction

President Obama released a $3.77 trillion fiscal year (FY) 2014 federal budget on April 10, 2013, with a mix of individual and business tax proposals intended to raise revenue, reduce spending and encourage negotiations between the White House and the GOP on comprehensive tax reform. President Obama called for a 28 percent cap on itemized deductions, a $3 million limit on tax-preferred retirement savings, a permanent research tax credit, a permanent American Opportunity Tax Credit (AOTC), a change in the taxation of carried interest, and more. President Obama also provided for the first time specifics on the so-called Buffet Rule. Following release of the President's FY 2014 budget recommendations, the Treasury Department issued its customary "Green Book," describing the proposals.

IMPACT. *Administration officials have indicated that the President's proposals aim to draw in Republicans to possibly reach a "Grand Bargain" on taxes and spending. "The President stands by the compromise offer he made to Speaker John Boehner, R-Ohio, during 'fiscal cliff' negotiations in December 2012," the White House said in a statement after release of the FY 2014 budget. "The (FY 2014) budget includes all of the proposals in that offer, which would achieve $1.8 trillion in additional deficit reduction over the next 10 years, bringing total deficit reduction to $4.3 trillion."*

IMPACT. *Entitlement reform, which held up a grand bargain at the end of 2012, remains the greatest stumbling block. In a nod to the GOP, however, President Obama proposes to slow the growth of benefits by using a Chained Consumer Price Index (C-CPI-U), which would reduce overall spending and also raise revenue. Some observers foresee this concession as a game-changer, finally opening the door to the possibility of bipartisan negotiations that will eventually lead to comprehensive tax reform.*

Tax Reform. "Tax reform" has become a very popular phrase in Washington lately. Tax reform presents massive challenges before a bipartisan path to enactment may be found. But it also presents a signifi cant catalyst for compromise through which eff orts toward finding a "simpler and fairer" system are shared by both parties. All budgets now on the table—from the White House, the House and the Senate—put tax reform forward as a principal theme. Bipartisan House Ways and Means tax reform working groups and a series of discussion drafts are also now providing renewed momentum toward adopting a new Tax Code.

PRESIDENT OBAMA'S PROPOSALS

President Obama's FY 2014 recommendations carry many proposals made in previous budgets but also contain some new proposals that may be game changers. Previous proposals by the President to extend the Bush-era tax rates for all but higher-income taxpayers and make permanent the $1,000 child tax credit, for example, were enacted by ATRA.

INDIVIDUALS

Among the proposals for individuals in the President's FY 2014 budget are:

Limitation on Deductions. President Obama proposes to reduce the value to 28 percent of specified exclusions and deductions that would otherwise reduce taxable income in the 33, 35 percent and 39.6 percent income tax rate brackets. A similar limitation would apply under the AMT.

IMPACT. *Higher income individuals, effective January 1, 2013, are liable for the new 3.8 percent net investment income (NII) surtax and the new 0.9 percent Additional Medicare Tax. Both taxes were enacted by the PPACA and, despite protests from the GOP, are not expected to be repealed in the 113th Congress. Higher income individuals, effective after 2012, also are confronted with a revived limitation on itemized deductions ("Pease limitation") and revived personal exemption phaseout.*

IMPACT. *The proposed 28-percent cap on itemized deductions stands out as the most significant single revenue raiser within the President's budget, at $529 billion over 10 years. Democrats in the Senate apparently are weighing their support of the proposal. Senate Finance Committee member Benjamin Cardin, D-Md., recently indicated that members of his caucus could come around to support it. However, Cardin also indicated that it all depends on what happens with tax reform.*

Buffett Rule. For the first time, President Obama provides details about his so-called Buffett Rule. Individuals whose adjusted gross income exceeds $1 million would pay a minimum tax rate of 30 percent on the excess of the taxpayer's adjusted gross income over the taxpayer's modified charitable contribution deduction for the tax year (tentatively called the Fair Share Tax (FST)).

IMPACT. *The Green Book explains that the FST would be phased in starting at $1 million and would be fully applicable at $2 million. The $1 million and $2 million thresholds would be adjusted for inflation for tax years beginning after 2013.*

IMPACT. *Income that is reduced by deductions and credits is not the only target of the Buffett Rule. Capital gains that would ordinarily be taxed at a maximum 23.8 percent rate (20 percent net capital gain tax plus the 3.8 percent net investment income tax) are also effectively subject to an increased rate of 30 percent to the extent overall income exceeds the $1 million threshold.*

> "Administration officials have indicated that the President's proposals aim to draw in Republicans to possibly reach a 'Grand Bargain' on taxes and spending."

COMMENT. *In February, supporters of the Buffett Rule introduced the Paying a Fair Share Act of 2013 (Sen. 321). The Senate bill largely mirrors the President's proposal.*

Limit on Accrual of Retirement Benefits. President Obama proposes to limit contributions and accruals on tax-favored retirement benefits, including IRAs, qualified plans, tax-sheltered annuities, and deferred compensation plans. The limit would apply when a taxpayer accumulates total retirement amounts that exceed the amount necessary to provide the maximum annuity permitted for a defined benefit plan (generally, an annual benefit of $205,000, payable as a joint and 100 percent survivor annuity, starting at age 62). Currently, the maximum permitted accumulation would be approximately $3.4 million for an individual the age of 62.

IMPACT. *Treasury's Green Book notes that an excise tax on excess distributions from all qualified plans applied between 1986 and 1997, until it was repealed. According to the White House, current law does not adequately limit the amount a taxpayer can accumulate through multiple tax-favored plans. These accumulations exceed amounts that fund reasonable consumption and that justify tax-favored treatment, the administration cautions.*

COMMENT. *The limit would be determined at the end of the calendar year and would apply to contributions and accruals for the next calendar year. While no further contributions or accruals would be permitted, the taxpayer's account balance could grow from investment earnings and gains. Additional contributions would be permitted if the investment returns were less than a specified actuarial calculation.*

Estate and Gift Taxes. The American Taxpayer Relief Act (ATRA) permanently provided for a maximum unified federal estate and gift tax rate of 40 percent with an inflation-adjusted $5 million exclusion for estates of decedents dying after December 31, 2012. In ATRA negotiations, President Obama had pressed for a return to a 2009 structure, which calls for a 45 percent rate, with a $3.5 million estate tax exclusion and a $1 million lifetime gift tax exclusion (both indexed for inflation). The President's FY 2014 budget calls for the reinstatement of the 2009 estate and gift tax rates and exclusions, but not to begin until 2018. As under ATRA, however, portability of unused estate and gift tax exclusions between spouses would be allowed.

IMPACT. *A senior Treasury official said in Washington, D.C. on April 10 during a news conference on the Green Book that "A $3.5-million exemption is the right thing to do." The official echoed the administration's observation that, "We need an estate tax law that is fair and raises an appropriate amount of revenue." In contrast, some in Congress have been calling for a complete elimination of the estate tax under the rationale that it does not raise enough revenue proportionate to its cost of administration.*

Education. President Obama proposes to make permanent the AOTC. Under current law, the AOTC is scheduled to expire after 2017.

IMPACT. *Unlike the HOPE Credit, which the AOTC replaced, the AOTC applies to the first four years of a student's post-secondary education. The AOTC rewards qualified taxpayers with a tax credit of 100 percent of the first $2,000 of qualified tuition and related expenses and 25 percent of the next $2,000, for a total maximum credit of $2,500 per eligible student.*

Child Tax Credit. ATRA extended permanently the $1,000 child tax credit. However, the provision that reduces the earnings threshold for the refundable portion of the child tax credit to $3,000 is extended through 2017. President Obama proposes to make permanent this provision.

Child and Dependent Care Credit. President Obama proposes to permanently increase the AGI level at which the child and dependent care credit begins to phase down to $75,000 for tax years beginning after December 31, 2013.

Saver's Credit. As in previous budgets, President Obama proposes to make the saver's credit refundable.

Home Mortgage Cancellation Exclusion. President Obama proposes to extend through 2015 the exclusion of cancellation of indebtedness income on a taxpayer's principal residence (limited to $2 million). Under ATRA, this exclusion will expire at the end of 2013.

Tax Extenders for Individuals. Unlike previous budgets, President Obama did not propose the wholesale extension of the individual (and business) tax extenders, many of which are scheduled to expire after 2013. Instead, the President proposes to make permanent some of the individual extenders (such as the AOTC and the exclusion for cancellation of home mortgage debt, described above) and to leave the fate of others to tax reform.

WHAT'S NEW IN ADMINISTRATION'S (FY) 2014 BUDGET?

President Obama's fiscal year (FY) 2014 federal budget proposals contain approximately 160 separate tax provisions, of which 35 are new or significantly revised from last year's budget proposals, according to a senior Treasury Department official.

Highlights of new provisions include:

- Replacing the Consumer Price Index with the Chained-CPI
- Specifying implementation of the Buffett Rule through a new Fair Share Tax
- Capping amount contributed to tax-preferred retirement plans
- Providing a 10 percent tax credit to qualified employers for new jobs and wage increases
- Requiring derivative contracts to be marked to market with resulting ordinary gain/loss

IMPACT. *Some popular extenders, such as the state and local sales tax deduction and the teachers' classroom expense deduction, may be rolled up into a year-end tax bill if broader agreement on tax reform cannot be reached in the meantime.*

SMALL BUSINESSES

The President's FY 2014 budget includes a number of provisions the administration touts as aiding small businesses. Many of the proposals would also benefit businesses of larger size.

COMMENT. *In a break with past budgets, the President did not propose to extend bonus depreciation generally. He does propose 100-percent first year depreciation, however, for certain qualified property placed in service within a geographic "empowerment zone." Fifty percent bonus depreciation is scheduled to sunset after 2013 (after 2014 for certain longer-lived and transportation property).*

Code Sec. 179 Expensing. The Code Sec. 179 dollar limit for tax years 2012 and 2013 is $500,000 with a $2 million investment limit. President Obama proposes to make permanent and adjust for inflation the $500,000/$2 million thresholds for qualified property placed in service in tax years beginning after December 31, 2013.

IMPACT. *Qualified property would include off-the-shelf computer software but would exclude real property.*

Tax Credit for Job Creation. President Obama proposes a temporary 10 percent tax credit for qualified employers that create new jobs, increase wages or both. The maximum credit would be $500,000 and would be effective for wages paid during the 12-month period beginning on the date of enactment.

IMPACT. *The tax credit would be available to firms with annual wages below $20 million in 2012. The proposal would also provide a similar credit to tax-exempt employers.*

Qualified Small Business Stock. The President's proposal would make permanent the temporary 100 percent exclusion for qualified small business stock (QSBS) acquired after December 31, 2013. The AMT preference for gain excluded under the small business stock provision would also be repealed for all excluded small business stock gain.

COMMENT. *Treasury's Green Book is silent on whether the QSBS exclusion would carry forward to prevent QSBS gain nevertheless from being caught within the 30 percent Buffet rule tax.*

Start-Up Expenses. President Obama proposes to make permanent the temporary enhanced deduction for qualified start-up expenses ($10,000 reduced but not below zero by the amount expenses exceed $60,000).

UNICAP Rules. The President's proposal would exempt employers with average annual gross receipts of $10 million or less from the uniform capitalization (UNICAP) rules for costs incurred to produce real or personal property for use by the taxpayer in its trade or business for tax years beginning after December 31, 2013.

Code Sec. 45R Credit. The President's proposal would expand the Code Sec. 45R small employer health insurance tax credit to cover employers with up to 50 full-time equivalent (FTEs) employees, with a phase-out beginning at 20 FTEs for tax years beginning after December 31, 2012.

Retirement Plans. Small employers without qualified retirement plans would be required to offer automatic enrollment in an IRA to their employees. Generally, the requirement would apply to small employers in business for at least two years that have more than 10 employees. Small employers with fewer than 100 employees would also be eligible for a temporary non-refundable tax credit to help offset the costs of setting-up an automatic IRA arrangement. These and related changes would be effective for tax years beginning after December 14, 2014.

MORE BUSINESS PROPOSALS

Among the other business proposals in the President's FY 2014 budget are:

Carried Interest. Carried interest in an investment partnership would be designated as a services partnership interest under the President's proposals. A partner's share of services partnership interest that is not attributable to invested capital would be taxed as ordinary income. Self-employment tax would attach to this income.

IMPACT. *The President's proposal would apply regardless of the character of the income at the partnership level.*

LIFO Repeal. The President proposes to repeal the last-in, first-out (LIFO) method of accounting. Additionally, the President calls for repeal of the lower-of-cost-or-market (LCM) method of accounting.

IMPACT. *As in past budgets, repeal of these two accounting methods is estimated to be among the largest revenue raisers: at $80.8 billion over 10 years.*

WOTC. ATRA extended the Work Opportunity Tax Credit (WOTC) (and its enhancements for veterans). President Obama proposes to make permanent the WOTC, including the enhancements for veterans.

IMPACT. *Under the WOTC umbrella, the Returning Heroes Tax Credit provides up to $5,600 to employers that hire qualified unemployed veterans and the Wounded Warrior Tax Credit provides up to $9,600 to hire long-term unemployed veterans with service-connected disabilities.*

FUTA surtax. President Obama proposes to reinstate the 0.2 percent surtax under the Federal Unemployment Tax Act (FUTA), which expired July 1, 2011, and make the surtax permanent.

Business Tax Extenders. As with the individual business tax extenders, the President does not propose to extend all of the expiring business tax extenders. Instead, the President identified certain extenders, such as the research tax credit (discussed below), which would be made permanent.

LOOPHOLE CLOSERS

The President's FY 2014 budget includes a number of provisions designated as "loophole closures," including:

Corporate Jets. President Obama would harmonize recovery periods by allowing depreciation of general aviation passenger aircraft over a seven-year period. Noncommercial aircraft not carrying passengers and helicopters could still use the five-year period.

Punitive Damages. Punitive damages are deductible unless they are paid to a governmental entity or stem from a violation of antitrust law. The President's proposal would deny a deduction for punitive damages, whether from a judgment or settlement.

COMMENT. *If an insurer pays the punitive damages, the amount paid would be included in the party's gross income.*

ESOPs. Under current law, corporations cannot deduct dividends paid to shareholders. However, under certain conditions, C corporations can deduct dividends paid on employer stock held in an employee stock ownership plan (ESOP). The President's proposal would repeal the deduction for dividends paid on employer stock in an ESOP, where the ESOP is sponsored by a C corporation. An exception would be provided for C corporations with annual receipts of $5 million or less.

COMMENT. *While the current provision encourages investment in employer stock through ESOPs, the White House cautioned that it also subjects retirement benefits to increased risk.*

More Loophole Closers. The President also proposes to:

- Repeal the boot-within-gain limitation for distributions received in reorganization transactions if the exchange has the effect of the distribution of a dividend.
- Amend the partnership rules to expand the definition of a built-in loss, to prevent the duplication of losses.
- Extend the partnership basis limitation rules to certain nondeductible expenses.
- Limit the importation of losses under related-party loss limitation rules

MANUFACTURING AND INSOURCING

The President's FY 2014 budget includes a number of incentives to encourage business activity, including:

Research Credit. Under current law, the research credit will expire after December 31, 2013. President Obama proposes to make permanent the research credit and increase the alternative simplified credit to 17 percent.

IMPACT. *The White House and many in Congress believe that businesses need the certainty of a permanent credit to make adequate investments in R&D. The principal obstacle to making the credit permanent is its cost. Once again, its 10-year revenue estimate of $99.3 billion will make this proposal a hard sell in the face of deficit reduction, absent being rolled into more broad-based tax reform.*

Manufacturing Communities Tax Credit. President Obama proposes a new tax credit to support investments in communities that suffer a major job loss event and plans to develop appropriate selection criteria for investments. The proposal would provide $2 billion in credits for investments approved each year in 2014-2016.

Insourcing and Outsourcing. The President's proposal would create a new general business credit of 20 percent of eligible expenses paid to insource a U.S. trade or business. The proposal would also disallow deductions for expenses to outsource a U.S. trade or business, meaning actions to reduce a U.S. business and increase a foreign business that result in a loss of U.S. jobs.

COMMENT. *Treasury's Green Book explains that insourcing means reducing a business conducted outside the U.S. and starting or expanding the same business in the U.S., if this action increases U.S. jobs.*

INVESTMENT IN INFRASTRUCTURE/ REGIONAL GROWTH

President Obama proposes a number of incentives to encourage investment in infrastructure, including:

America Fast Forward Bonds. The President's proposal would create a new, permanent bond program that builds on the example offset by the Build America Bond program. Rather than tax-exempt bonds, the interest would be taxable (requiring issuers to pay higher rates), but the federal government would pay a 28 percent subsidy to state and local government issuers.

IMPACT. *Eligible uses would include government capital projects, refunds of prior public capital projects, short-term working capital financings, and financing for Code Sec. 501(c)(3) organizations, such as hospitals and universities. Eligible uses would also include programs financed with qualified private activity bonds, such as low- and moderate-income housing. Another proposal would provide a temporary 50 percent subsidy rate for 2014 and 2015 bonds used for school construction, including public schools and state universities.*

IMPACT. *The President also proposes tax-favored bonds (exempt interest or tax-credit bonds) to allow state and local governments, nonprofit organizations, and certain other entities to raise funds for various public purposes.*

Real Property Interests. The President's proposal would exempt from FIRPTA (the Foreign Investment in Real Property Tax Act) any gains realized by foreign pension funds from the disposition of U.S. real property interests. U.S. pension funds are not taxable on these gains, but gains of a similar pension fund created outside the U.S. are currently taxable under FIRPTA.

New Markets Tax Credit (NMTC). The NMTC is scheduled to expire on December 31, 2013. President Obama proposes to extend the NMTC permanently, with an allocation of $5 billion in credits annually.

IMPACT. *The credit can offset regular tax liability but not AMT liability.*

Low-Income Housing Tax Credit (LIHTC). The President's FY 2014 budget includes proposals regarding the LIHTC, designed to expand the impact of the credit. These proposals would allow states to convert private activity bond caps into tax credits, encourage mixed-income occupancy by loosening criteria on occupants' average income, and use existing federal housing to increase the supply of affordable housing.

REVENUE RAISERS

Top revenue raisers in the FY 2014 budget (based on Green Book estimates) include:*

28 Percent Cap on Deductions and Credits	$529
Use of Chained Consumer Price Index	$100
Repeal of LIFO	$80.8
Tobacco Tax Increase	$78.0
Estate/Gift Tax at 2009 Levels	$71.6
Foreign Tax Credit on Pooling Basis	$65.7
Financial Crisis Responsibility Fee	$59.3
Buffett Rule/Fair Share Tax	$53.3

* In billions of dollars, over 10 years

Note: Some proposals, although "high-profile," would raise only a limited amount of revenue: for example, $15.9B from taxing carried interest.

And More. Among other proposals, the President's FY 2014 budget would:

- Repeal the $150 million limit on non-hospital bonds used by Code Sec. 501(c)(3) organizations;
- Increase by $4 billion the national limit for tax-exempt private activity bonds used to finance highway or surface freight transfer facilities, including bridges and tunnels;
- Eliminate the volume cap for private-activity bonds used for water and wastewater infrastructure facilities; and
- Increase the percentage of private activity bond proceeds that can be used for land acquisition.

ENERGY INCENTIVES

A number of proposals in the President's FY 2014 budget would encourage the production and use of "clean energy," including:

Advanced Technology Vehicles. The President's proposal would replace the plug-in electric vehicle credit with a credit for advanced technology vehicles that operate primarily on an alternative to petroleum. The credit would be $5,000-$10,000 per vehicle and would be allowed to the person who sells the vehicle

> **COMMENT.** *The credit would be available for vehicles placed in service before 2021 and would be phased out over the last three years.*

Alternative Fuel Vehicles. The President proposes a credit to the buyer of medium- and heavy-duty commercial vehicles (trucks) that use alternative fuels. The credit could be as high as $25,000 for vehicles weighing 14,000-26,000 pounds, and as high as $40,000 for heavier vehicles.

Renewable Electricity Production Tax Credit. The renewable electricity production tax credit, for energy produced from wind, biomass, geothermal resources, and other sources, is temporary. The administration proposes to permanently extend the credit and make it refundable.

Energy Efficient Buildings. The President's proposal would enhance the deduction allowed for the costs of energy efficient commercial buildings, which is primarily used in connection with new buildings. The proposal would also provide a new deduction for retrofitting existing commercial buildings.

Fossil Fuels. The President proposes to repeal numerous tax benefits available to oil, gas and coal producers for tax years beginning after December 31, 2013, including the enhanced oil recovery credit, the credit for oil and gas produced from marginal wells, expensing of exploration and development costs, and more.

> **IMPACT.** *Repeal of the fossil fuel preferences is estimated to raise $43.9 billion over 10 years.*

INTERNATIONAL PROPOSALS

Obama's FY 2014 budget proposals on international taxation retain similar budget proposals (11 in all) from FY 2013, including:

Transfers of Intangibles. If a U.S. person transfers an intangible asset from the U.S. to a related controlled foreign corporation (CFC), excess income from transactions connected to the intangible would be treated as Subpart F income that is currently taxable in the U.S., if the income is subject to a low foreign effective tax rate of 10 percent or less. The President's proposal would phase out for effective tax rates of 10 to 15 percent. The President also proposes clarifying the definition of intangible property to include workforce in place, goodwill, and going concern value.

> **IMPACT.** *Treasury's Green Book explains that income shifting through transfers of intangibles to low-taxed affiliates has significantly eroded the U.S. tax base. Taxpayers also avoid U.S. taxes by providing a low value for intangibles transferred between related persons.*

Interest Expense. President Obama proposes to defer the deduction of interest expense that exceeds the taxpayer's pro rata share of income from foreign subsidiaries that is subject to current U.S. tax. The interest would be deductible in a later year. The proposal would prevent a U.S. person that incurs debt to acquire foreign stock from currently deducting the interest expense, even if the expenses exceed foreign source income or if the taxpayer earns no foreign source income.

Foreign Tax Credits. The President's proposal would require that a deemed paid foreign tax credit would be limited to an amount proportional to the pro rata share of earnings and profits of foreign subsidiaries that are repatriated to the U.S. taxpayer and taxable currently. The foreign tax credit would be determined on a consolidated basis, by taking into account the aggregate foreign taxes and earnings and profits of all foreign subsidiaries for which the U.S. taxpayer can claim a deemed paid foreign tax credit. Another proposal would reduce the foreign taxes paid through foreign tax pooling where foreign earnings and profits are eliminated.

Earnings Stripping. Opportunities are available to reduce U.S. taxes on income earned from U.S. operations through the use of foreign related-party debt. The President's proposal would tighten the limitation on deducting interest paid by an expatriated entity to related persons.

> **IMPACT.** *Code Sec. 163(j) limits the deduction of interest paid by a corporation to a related person. According to the White House, some taxpayers are using the deductions to inappropriately reduce their taxes on income earned from U.S. operations.*

Reinsurance Premiums. Insurance companies can deduct premiums paid for reinsurance. Nontaxable reinsurance transactions

SEQUESTRATION SOLUTION?

The President's budget would replace sequestration (across-the-board spending cuts under the Budget Control Act of 2011 and subsequent legislation) for FY 2014 but not for the remainder of FY 2013. As a result, the IRS's plans to furlough employees five to seven days before the end of FY 2013 are likely to move forward. Furloughs are expected to begin sometime this summer and the impact on return processing, refunds, collections, and enforcement is uncharted territory for an agency already under budgetary pressure to do more with less.

with foreign affiliates can result in substantial U.S. tax advantages. The President's proposal would deny a deduction for premiums and other amounts paid to affiliated foreign companies if the foreign reinsurer is not subject to U.S. taxes on the premiums received.

TAX GAP

As in past years, the FY 2014 budget includes many proposals to reduce the tax gap (the difference between what taxpayers owe and what they pay). The FY 2014 budget includes over 30 provisions design to close the tax gap, including:

IRS Budget. President Obama proposes to increase funding for the IRS by more than eight percent for FY 2014. Overall, the President would request approximately $12.9 billion to fund the IRS in FY 2014.

IMPACT. *Through the end of FY 2013, the IRS is operating under FY 2012 budget parameters and sequestration. Sequestration has reduced the IRS's budget for the remainder of FY 2013 by approximately $600 million, according to the agency.*

COMMENT. *The President also proposes adjusting the IRS's discretionary spending limits for FY 2014 to fund new revenue producing initiatives through the use of a budget mechanism called a program integrity cap adjustment. For FY 2014, the adjustment would fund over $400 million in new enforcement and compliance programs.*

COMMENT. *Beginning in 2014, the IRS will oversee two far-reaching provisions in the Patient Protection and Affordable Care Act: the individual mandate and the employer shared responsibility requirement.*

Identity Theft. The President's proposal would impose a $5,000 civil penalty, for each incidence, on individuals who file a return using another taxpayer's identity. There would be no maximum amount that could be imposed. The President also proposes to add tax-related offenses to the Aggravated Identity Theft Statute.

IMPACT. *On the same day that President Obama released his FY 2014 budget, the Treasury Inspector General for Tax Administration (TIGTA) told a Senate committee that the IRS identified almost 1.8 million incidents of identity theft in calendar year 2012. The IRS stopped the issuance of $12.1 billion potentially fraudulent tax refunds associated with 1.8 million returns classified as involving identity theft.*

Penalties. The President calls for indexing all IRS penalties for inflation. This change would be effective upon enactment.

IMPACT. *The President did not propose comprehensive review of the IRS's overall penalty framework as many in the tax community have proposed.*

Exempt Organizations. The President's proposal would require all tax-exempt organizations that file Form 990, Return of Organization Exempt from Income Tax, to file that form electronically. The requirement would be effective for tax years beginning after the date of enactment.

Levy. The President's budget would allow the IRS to levy up to 100 percent of a payment to a Medicare provider to collect unpaid taxes.

HOUSE AND SENATE BUDGET PROPOSALS

In March, the House and Senate approved nonbinding budget resolutions. This is the first time in a number of years that both the House and Senate have approved budget resolutions. The parties, however, remain far apart. But while the differences are said to be "irreconcilable," informal negotiations may already be taking place.

IMPACT. *If the White House and the GOP can agree on reductions in entitlement programs, prospects for a grand bargain over taxes and spending will greatly improve. President Obama's proposal to adopt a Chained-CPI could help win support from Republicans for comprehensive tax reform.*

HOUSE GOP BUDGET PROPOSALS

The House GOP proposals were unveiled in *The Path to Prosperity: A Responsible, Balanced Budget, The House Republican Fiscal Year 2014 Budget Resolution.* The GOP budget would achieve $4.6 trillion in spending cuts over 10 years, with no new tax revenues. The budget would balance in 2023, according to GOP projections. The House approved the GOP budget resolution on March 21 by a 221-207 vote.

The House GOP budget proposes three tax reform goals:

- Simplify the Tax Code,
- Make the tax laws fairer to families and businesses, and
- Reduce the amount of time and resources necessary to comply with the tax laws.

COMMENT. *The GOP budget proposal would reform the Tax Code, but would be revenue-neutral and would not raise any new tax revenues. Rep. Paul Ryan, R-Wisc., chair of the House Budget Committee, noted that the Congressional Budget Office estimated total government revenues of $40.2 trillion under the current Tax Code for the period 2014-2023. Ryan's budget would maintain that estimated amount of revenue, but would not raise any additional revenue.*

Individuals

Tax Rates. The House GOP proposal would consolidate the seven current individual income tax rate brackets (10, 15, 25, 28, 33, 35, and 39.6 percent) into two rates. The lower rate would be 10 percent, and the budget supports lowering the higher tax rates for individuals, with the goal being a top rate of 25 percent.

COMMENT. *ATRA made the Bush-era tax rates permanent, starting in 2013, for most taxpayers. Those with incomes above particular thresholds, however, are now taxed at a 39.6 percent rate under ATRA: $400,000 for individuals; $425,000 for heads of households; and $450,000 for married taxpayers filing jointly and surviving spouses. The capital gains rate for higher income individuals, trusts and estates also increased from 15 percent to 20 percent.*

COMMENT. *The GOP budget would repeal the 3.8 percent surtax on net investment income and the 0.9 percent Additional Medicare Tax, both of which took effect January 1, 2013. Short of a general repeal of the health care reform law, however, elimination of these new sources of tax revenue is deemed highly unlikely by most Washington observers.*

Alternative Minimum Tax. The House GOP would repeal the AMT.

IMPACT. *The AMT is a significant revenue raiser. President Obama proposed to offset the loss of revenue from AMT repeal with the so-called Buffett rule on incomes above $1 million. The GOP plan would count the general revenue increase gained from a more streamlined Tax Code as providing a sufficient offset.*

Itemized Deductions. The House GOP proposal to simplify the Tax Code and reduce the amount of time and resources necessary to comply with the tax laws includes an examination of itemized deductions. The GOP did not provide specifics of simplification or burden reduction.

IMPACT. *While the GOP's goal for higher-income taxpayers is to lower their overall tax rates, Republicans are not united in examining what tradeoffs need to be considered. For example, real estate lobbyists have already made noise about further caps on the mortgage interest deduction (or transforming it into a credit), and charities are concerned that contributions would drop precipitously should the itemized deduction for charitable contributions be curtailed.*

Businesses

The GOP budget would reduce the top corporate tax rate to 25 percent and would transition the Tax Code to a purportedly more competitive system of international taxation, a territorial approach for taxing multinational corporations. *See discussion of corporate tax rates, within the context of the House Ways and Means discussion draft on International Competitiveness, later in this Tax Briefing.*

SENATE DEMOCRATIC BUDGET PROPOSALS

The Senate approved a FY 2014 budget resolution on March 23: *Foundation for Growth: Restoring the Promise of American Opportunity*. The Senate budget would cut the deficit by $1.85 trillion over 10 years, by providing $975 billion in new revenues, $975 billion in spending cuts, and a $100 billion investment in jobs and infrastructure.

IMPACT. *The Senate budget instructs the Senate Finance Committee to develop proposals to raise $975 billion in new tax revenues and report tax legislation by October 1, 2013. This legislation would not be subject to Senate filibuster; under budget reconciliation rules, so only 50 votes would be needed to enact it.*

Middle Class Relief. The Senate budget would extend the "middle class tax relief" in ATRA, including support for education through a permanent extension of the AOTC. The Democratic budget would also "protect and continue tax cuts for the middle class and low-income working families." The budget explains in general terms that it would not increase the tax burden on the middle class or "the most vulnerable Americans," and would obtain tax savings "only from the wealthiest Americans and biggest corporations." The Senate budget "supports the goal of comprehensive tax reform … if it is done in a way that is consistent with the revenue and progressivity goals of this budget."

IMPACT. *Thus, the Senate Democratic budget does not necessarily call for comprehensive tax reform at this time. It supports measures to end loopholes and "wasteful" tax expenditures. At the same time, it states that "the current state of the Tax Code is simply indefensible. It is unfair, inefficient, and it is hurting the competitive position of U.S. businesses."*

Tax Reform Principles. Tax reform, according to Democratic budget guidelines, should restore fairness and boost economic growth by adhering to the following principles:

- Maintain progressivity, including enhanced tax credits for low-income and middle class families;
- Aggressively address the tax gap and offshore tax abuse;
- Eliminate unfair and inefficient business tax loopholes;
- Increase certainty and simplify the Tax Code;
- Reform business taxes to help U.S. enterprises compete and ensure that America remains the best place to start a business and create jobs; and
- Reduce tax rates responsibly, but only if revenue and progressivity goals are achieved or maintained.

Reducing Tax Expenditures. The Democratic budget is short on many specifics, but would generally:

- Impose across-the-board limits on itemized deductions claimed by the top two percent of income earners, by capping the rate at which itemized deductions and other tax preferences reduce tax liability, a percentage of income cap, or a specific dollar cap.
- Reform the structure of tax expenditures, for example, by converting unspecified itemized deductions into itemized credits.

- Impose a higher tax rate on carried interest;
- End special depreciation rules for corporate jets; and
- Eliminate offshore tax shelters and remove incentives for companies to move assets offshore. The budget refers to shifting profit-generating assets offshore through abusive transfer pricing transactions, manipulating the source of dividend payments, or incorporating in a tax haven.

Other Senate Votes. The Senate also approved nonbinding resolutions this year to repeal the PPACA's tax on medical devices in a deficit-neutral manner, eliminate the $2,500 cap on health care flexible spending accounts, and approve the Congressional Budget Office's use of dynamic scoring of tax legislation.

CONGRESSIONAL WORKING GROUPS

Both the Senate Finance Committee (SFC) and the House Ways and Means Committee have been working on tax reform for the past two years. "We know we face some fierce headwinds …[but] tax reform can't be about politics. It has to be about the people we serve…," Sen. Max Baucus, D-Mont., chair of the SFC and Rep. Dave Camp, R-Mich., chair of the Ways and Means Committee, said in a joint statement.

WAYS AND MEANS TAX REFORM DISCUSSION DRAFTS

The House Ways and Means Committee has released three major discussion drafts so far on tax reform relating to:

- Small businesses,
- Financial products and
- Moving the U.S. to a territorial system of taxation/reduced corporate tax rates.

A summary of each of the three discussion drafts appears, below.

COMMENT. *Rep. Camp has promised that the committee will move tax reform legislation in 2013. The committee has a wealth of proposals for tax reform from many hearings in the 112th Congress and more in the current Congress. Camp has said that he will not allow specific portions of the reports to move as stand-alone bills, in part because the goal of overall revenue neutrality can be more easily achieved through a larger pool of provisions.*

> "The House GOP proposal would consolidate the seven current individual income tax rate brackets into two rates."

COMMENT. *It is unclear to what extent the House leadership is on board with moving comprehensive tax reform legislation in 2013. Nonetheless, the committee's discussion drafts are among the most detailed proposals for tax reform currently released by lawmakers, particularly in contrast to the proposals released by the House and Senate Budget Committees.*

Working Groups. The House Ways and Means Committee has also organized 11 bipartisan working groups to review and propose reforms to the Tax Code within designated issue areas:

- Charitable/Exempt Organizations
- Debt, Equity and Capital
- Education and Family Benefits
- Energy
- Financial Services
- Income and Tax Distribution
- International
- Manufacturing
- Pensions/Retirement
- Real Estate
- Small Business/Passthroughs

COMMENT. *Based in part on the findings of each of these groups, which are due by April 15, 2013, the Joint Committee on Taxation has been charged with preparing a report that "describes current law in each issue area and summarizes the other information gathered by the Committee Members." The report is due by May 6, 2013.*

COMMENT. *In addition to the working groups on tax reform, over 20 hearings have taken place since 2011 on a variety of tax-reform topics, including Small Businesses and Tax Reform (March 3, 2011), Tax Burdens on Individuals and Families, (April 13, 2011), Interaction of Tax and Financial Accounting on Tax Reform (February 8, 2012), Tax Reform and the U.S. Manufacturing Sector (July 19, 2012), and the Charitable Contributions Deduction (February 14, 2013), among others.*

Small Business Proposals

In March 2013, the Ways and Means Committee released a discussion draft of small business tax proposals. Although the committee labeled the draft "small business," some of the proposals would reach large businesses.

INFORMATION REPORTING NEVER FAR AWAY

Although Congress has rolled back some information reporting requirements, information reporting remains popular among lawmakers because it is predicted to enhance tax compliance. In the Senate, there have been discussions about requiring information reporting by federal, state, and local governments on non-wage payments for property or services and requiring life insurance companies to report certain transactions, including sales, transfers, and benefits.

TIMELINE
2013 TAX REFORM DEVELOPMENTS

January 24	House Ways & Means Committee Chair Dave Camp, R-Mich., releases a discussion draft on comprehensive tax reform of financial products
February 5	President Obama proposes package of spending cuts to Medicare/ other programs, balanced against revenue-raising tax reforms
February 11	Senate Democrats reintroduce the Cut Unjustified Tax Loopholes Act (Sen 268)
February 13	Formation of 11 separate Ways and Means Committee Tax Reform Working Groups
February 13	Sen. Sheldon Whitehouse, D-R.I., introduces the Paying a Fair Share Act of 2013 (Sen. 321), which would implement the Buffett Rule.
February 19	Authors of the 2010 Simpson–Bowles Plan for tax reform, release revised proposal calling for additional $2.4 trillion in federal debt reduction
February 26	Sen. Harry Reid, D-Nev., introduces Sen. 388 that proposes an average 30 percent tax rate for taxpayers with income more than $5 million
February 27	Senate Republicans introduce a bill (Sen 16) that would effectively require the President to cancel the upcoming sequester and issue a plan for its replacement.
February 28	Both the Democratic and Republican bills to prevent sequestration cuts fail
March 6	The House passes a continuing resolution (HR 993) to prevent a government shutdown and continue operations through September 30, 2013.
March 12	Rep. Paul Ryan, R-Wis., releases the Republican 2014 fiscal year (FY) budget resolution
March 13	Sen. Patty Murray, D-Wash., releases the Democrats' FY 2014 budget resolution
March 14	The Senate Budget Committee approves the Democratic version of the FY 2014 budget resolution
March 21	The House passes the Republican version of FY 2014 budget resolution
March 23	The Senate passes Democratic version of FY 2014 budget resolution
April 10	President Obama releases his FY 2014 budget proposals
May 6	Joint Committee on Taxation to report on tax reform
May 18	Federal Debt Limit reached (Treasury may extend until August)
September 30	Federal Government funding expires at end of FY 2013
December 31	Many individual and business extenders expire after December 31, 2013

IMPACT. *In addition to enhancing certain tax benefits that are available to small businesses, the small business discussion draft makes sweeping proposals that could significantly alter the way in which partnerships, S corporations and LLCs are taxed in the future.*

Code Sec. 179 Expensing. The Ways and Means draft would establish a permanent Code Sec. 179 dollar limit of $250,000 with an $800,000 investment limit for tax years beginning after December 31, 2013. The temporary provision allowing expensing of off-the-shelf computer software would be made permanent. Additionally, qualified real property – generally qualified leasehold improvement property, restaurant property and retail improvement property—would be treated as Code Sec. 179 property.

Cash Method of Accounting. The Ways and Means draft would provide a uniform rule generally allowing all businesses satisfying a gross receipts test to use the cash method of accounting. The revised gross receipts test allows taxpayers with annual average gross receipts that do not exceed $10 million (up from the current $5 million) for the three prior tax-year period to use the cash receipts and disbursements method, so long as use of such method clearly reflects income, for tax years beginning after December 31, 2013.

The House Ways and Means draft would also coordinate the current rules for certain farming businesses, requiring them to use the nonaccrual method of accounting with the new general rule. The provision also expands the exception from the uniform capitalization rules -- a taxpayer that produces tangible personal property and has $10 million or less of average annual gross receipts is not subject to Code Sec. 263A.

IMPACT. *Ways and Means acknowledged that it has not addressed the possible impact of expanding the cash method on other provisions of the Code not directly related to accounting methods.*

Start-Up Expenses. The Ways and Means draft would consolidate the current rules for start-up expenses and organizational expenditures into one provision, effective for expenses paid or incurred after December 31, 2013. A qualified taxpayer could deduct up to $10,000 of the sum of start-up and organizational expenditures in the taxable year in which the active trade or business begins. The $10,000 amount would be reduced (but not below zero) by the amount by which the cumulative cost of the sum of start-up and organizational expenditures would exceed $60,000. Remaining expenditures would be amortized over a period of not less than 180 months.

Filing Due Dates. The Ways and Means draft would move back the original filing date of federal income tax returns of partnerships and move forward the original filing date of federal income tax returns of C corporations and S corporations:

- Partnership returns would be filed on or before the 15th day of the third month following the close of the taxpayer's tax year, or March 15 in the case of a calendar year taxpayer;
- S corporation returns would be filed on or before the last day of the third month following the close of the corporation's tax year, or March 31 in the case of a calendar year taxpayer; and
- C corporation returns would be filed on or before the 15th day of the fourth month after the close of a tax year, or April 15 in the case of a calendar year taxpayer.

The changes would be effective for returns for tax years beginning after December 31, 2013.

> **IMPACT.** *Late Schedule K-1s are a growing problem. Many taxpayers do not receive their K-1s until the middle or end of March or even April. The Ways and Means draft would aim to encourage more taxpayers to file by the regular due dates rather than seeking extensions. The Senate Finance Committee has recommended a similar set of deadlines.*

> **COMMENT.** *The House Ways and Means draft would also make the due date of Form TD F 90-22.1 ("FBAR)" April 15 rather than the current June 30.*

Partnerships and S Corporations. The Ways and Means draft presents two options for reform of partnerships and S corporations, one relatively conservative ("Option 1") and the other more radical in scope ("Option 2").

Option 1 for partnerships would:

- Repeal rules relating to guaranteed payments;
- Repeal rules relating to payments made in liquidation of retiring or deceased partner;
- Require mandatory adjustments to basis of partnership property in case of transfer of partnership interests or a partnership's distribution of property;
- Adjust the limitation on a partner's share of losses to take into account charitable contributions and foreign taxes;
- Clarify that distributions of inventory items are treated as a sale or exchange between the partner and the partnership; and
- Require that partners contributing property with built-in gains or losses be subject to tax on the pre-contribution gain or loss in certain circumstances.

Option 1 for S corporations would:

- Make permanent the five-year period for built-in gain;
- Simplify and extend the deadline for making an S corp election;
- Increase the portion of S corp income that may be passive from 25 percent to 60 percent;
- Eliminate termination of S status for excess passive income for three consecutive years;
- Allow non-resident aliens to be S corp shareholders through an electing small business trust (ESBT);
- Permit ESBTs to deduct charitable contributions made by the S corp; and
- Revise basis adjustments to S corp shares to encourage charitable contributions.

Option 2 for both partnerships and S corporations would:

- Repeal the current rules for partnerships and S corporations and impose a new unified pass-through regime that:
  - Allows start-up contributions of property and cash on a tax-free basis;
  - Maintains the character of income, gains, losses and credits that are passed through to owners;
  - Allows specific allocations to owners of net ordinary income or loss, net capital gain or loss, and tax credits only;
  - Prevents gaming the system by limiting loss deductions to an owner's basis in his pass-through interest (but allowing unlimited carryforwards);
  - Limits tax-free distributions to the owner's basis in the business; and
  - Allows owners to be treated as employees of the business.

> **IMPACT.** *Rather than offer a simplified system, Option 2 may add far more complexity, especially for many existing S corporations. A myriad of transition rules likely will need to be negotiated, and many S corp owners—who already operate under what they consider a relatively simple set of rules—are concerned that they may bear the brunt of reforming partnership taxation.*

> **IMPACT.** *Efforts to lower the corporate tax rate, if successful, could encourage more taxpayers to operate businesses in corporate form rather than as passthroughs. As a result, some observers have recommended that comprehensive reform address all rates at the same time.*

CONGRESS MAY REGULATE RETURN PREPARERS

In January, the U.S. District Court for the District of Columbia enjoined the IRS from implementing its return preparer oversight initiative (*Loving, 2013-1* USTC *¶50,156*). The initiative would have required unenrolled preparers to successfully pass mandatory testing, obtain continuing education and more. The IRS has appealed the district court's decision to the U.S. Court of Appeals for the District of Columbia Circuit. In the meantime, Congress may approve legislation that expressly grants the IRS authority to implement the return preparer requirements. The Senate Finance Committee made special note of the controversy in its first tax reform discussion draft.

Financial Products Taxation

In January, the Ways and Means Committee issued a discussion draft on the taxation of financial products. On March 20, the House Ways and Means Subcommittee on Select Revenue Measures considered the draft of financial products tax reform. The draft addresses derivatives, wash sales and more.

IMPACT. *This discussion draft has been singled out as a possible frontrunner for stand-alone tax reform legislation in 2013 if Congress cannot agree on broader tax reform at this time. Nevertheless, there is resistance to its provisions being passed as a one-time revenue raiser or tax increase rather than as part of a broader tax reform plan.*

Financial Derivatives. The Ways and Means draft generally would require all derivative positions (futures, forward contracts, swaps, and options) to be marked to market at the end of each tax year, effective for derivatives entered into after December 31, 2013. Each derivative held by a taxpayer would be treated as if it were sold on the last business day of the year for its fair market value, and any resulting gain or loss would be taken into account for such taxable year. For straddles (for example, offsetting financial positions) that include at least one derivative position, all positions would be marked to market with ordinary income or loss treatment.

IMPACT. *Some transactions involving derivatives (for example, hedges used by companies to mitigate the risk of price, currency and interest rate changes in their businesses and options to acquire real estate) would be exempt from the proposed changes.*

Wash Sales. The Ways and Means draft would extend the wash sale rules to acquisition of substantially identical stock or securities by the taxpayer or a related party for sales and dispositions after December 31, 2013. Additionally, the basis of the substantially identical stock or securities is not adjusted to include the disallowed loss in the case of any acquisition by a related party other than the taxpayer's spouse.

Business Hedging Tax Rules. Under the Ways and Means draft, taxpayers would be permitted for tax purposes to rely on an identification of a transaction as a hedge that they have made for financial accounting purposes.

Debt Restructurings. The Ways and Means draft would eliminate what the committee characterizes as "phantom" tax resulting from debt restructurings by providing that the issue price of the modified debt instrument cannot be less then the issue price of the debt instrument before modification.

Secondary Market Bonds. Purchasers of bonds at a discount on the secondary market would include, under the Ways and Means draft, the discount in taxable income over the post-purchase life of the bond, rather than only upon retirement of the bond or resale of the bond by the purchaser, effective for bonds acquired after December 31, 2013.

Identical Securities. Under the discussion draft, taxpayers who sell a portion of their holdings of the securities of a particular corporation would be required to determine their taxable gain or loss based on the taxpayer's average basis in the securities, including both the securities sold and the securities retained by the taxpayer, for sales of securities occurring after December 31, 2013.

International Competitiveness/ Corporate Tax Rate Reduction

The Ways and Means Committee released in 2011 a discussion draft about moving the U.S. from a worldwide system of taxation to a territorial system of taxation along with a reduction in the corporate tax rate.

Corporate Tax Rate. The Ways and Means draft would reduce the maximum corporate tax rate from 35 percent to 25 percent for tax years beginning after December 31, 2012.

IMPACT. *Many experts have testified that a reduction in the corporate rate could increase investment in the U.S. and reduce the incentive to move activities and income offshore, as well as make the U.S. a more attractive location for multinational corporations to locate their headquarters. The House-passed FY 2014 Budget proposes a 25 percent corporate tax rate. One rule of thumb currently being used within the debate over lowering the corporate tax rate is that a 1-percentage-point reduction in the rate costs $100 billion over 10 years.*

Foreign Business Income. The Ways and Means draft would establish a participation exemption system from U.S. taxation for foreign business income. The exemption would be effectuated by means of a 95 percent deduction for the foreign source portion of dividends received from controlled foreign corporations (CFCs) by domestic corporations that are 10 percent U.S. shareholders of those CFCs. No foreign tax credit would be allowed for any taxes (including withholding taxes) paid or accrued with respect to any dividend for which the 95 percent dividends-received deduction would be allowed.

COMMENT. *A domestic corporation would be allowed the 95 percent deduction for a dividend it receives on stock of a CFC only if the domestic corporation satisfies a one-year holding period requirement in respect of the stock on which the dividend is paid. No deduction would be allowed in respect of any dividend on any share of CFC stock that is held by the domestic corporation for 365 days or less during the 731-day period beginning on the date that is 365 days before the date on which the share becomes ex-dividend with respect to the dividend.*

SOME PPACA PROVISIONS COULD BE AMENDED

Although the House GOP FY 2014 budget calls for repeal of the Patient Protection and Affordable Care Act (PPACA), prospects for repeal are zero with Democrats in control of the Senate. However, some provisions of the PPACA could be repealed or amended, such as the new excise tax on medical devices. In March, the Senate overwhelmingly approved a non-binding resolution to repeal the medical device tax.

COMMENT. *Five percent of a dividend from a CFC would remain taxable. Ways and Means explained that this taxation is intended to be a substitute for the disallowance of deductions for expenses incurred to generate exempt foreign income.*

Transition Rule. The Ways and Means draft would apply a 5.25 percent tax (payable in eight annual installments) to all existing earnings currently held offshore, whether or not the earnings are repatriated. Once paid, the earnings would benefit from the 95 percent exemption if returned to the U.S.

COMMENT. *The Ways and Means draft also discusses subpart F, elimination of foreign tax credit baskets, anti-abuse rules, and a "thin capitalization rule" that would disallow a portion of net interest expense if a U.S. company that is a member of a worldwide group fails certain tests.*

SENATE FINANCE COMMITTEE TAX REFORM OPTIONS

The Senate Finance Committee, like the House Ways and Means Committee, has been exploring various options for tax reform. The SFC held numerous hearings in the 112th Congress about tax reform. In March 2013, the SFC issued the first of what is likely to be a series of discussion papers on tax reform options.

IMPACT. *SFC Chair Max Baucus, D-Mont., has set August 2013 as the deadline for his committee to produce a tax-reform plan. He has reiterated a commitment to work with House Ways and Means Chair, Dave Camp, R-Mich., in developing a tax reform bill with bipartisan support.*

COMMENT. *The SFC tax reform draft merely presents broad general outlines for possible tax reform, apparently leaving specifics for future discussions. The proposals do not reflect the official positions of Baucus or Ranking Member Orrin Hatch, R-Utah.*

IMPACT. *The SFC draft discusses a controversial proposal to have the IRS pre-fill returns and preliminarily calculate the tax due, if any, for simple returns (similar to California's "ReadyReturn" program). The taxpayer could either accept or reject this IRS-prepared return. The SFC draft does not describe a "simple return" or under what parameters the program would operate, such as limiting the program to single individuals or individuals only with income from wages.*

Tax Simplification. In the area of tax simplification, the SFC draft identifies areas for simplification (without endorsing any), such as simplification or repeal of the AMT, the personal exemption phaseout (PEP), the limitation on itemized deductions and the corporate AMT. Simplification could also be achieved by establishing uniform definitions of terms such as qualifying child, modified adjusted gross income and related party, and by consolidating similar penalties.

Information Reporting. The SFC draft identifies a number of potential ways to expand information reporting, including:

- Improved information reporting by financial institutions on unreported and underreported financial accounts
- Additional information reporting on home mortgage interest
- Mandatory reporting by life insurance companies of certain transactions, including sales, transfers and benefits

Compliance. The SFC draft describes proposals to limit the ability of seriously delinquent taxpayers to avoid paying taxes by:

- Revoking or denying passports to seriously delinquent taxpayers
- Requiring Medicare contractors to screen prospective Medicare providers for unpaid taxes
- Authorizing a 100 percent continuous levy on payments to Medicare providers and suppliers that neglect or refuse to pay taxes

Audit and Collection. The SFC draft identities a number of areas to improve the taxpayer experience in IRS audit and collection procedures, such as expanding virtual face-to-face audits, making it easier to structure payment plans with the IRS, and providing waivers for user fees when installment agreements use automated withdrawals.

COMMENT. *The IRS has implemented a number of reforms to installment agreements under its Fresh Start initiative, including raising the maximum dollar criteria for streamlined installment agreements from $25,000 to $50,000 and the maximum term from 60 months to 72 months.*

Filing Process. Along with changing due dates for certain returns (to ensure timely receipt of third-party information by taxpayers and the IRS), the SFC draft describes other proposals to improve the filing process, such as requiring electronically-prepared paper returns to include a 2D barcode, authorizing the IRS to use external data to verify employment, and extending the refund-due date beyond which the IRS must pay interest.

OTHER TAX LEGISLATION

Along with the House Ways and Means Committee and the Senate Finance Committee, some other committees and lawmakers have also proposed tax legislation. The House Oversight and Government Reform Committee in March approved the Federal Employee Tax Accountability Act of 2013 (HR 249) in March. The bill would prohibit the hiring of future federal employees who already have a seriously delinquent tax debt. The Committee also approved the Contracting and Tax Accountability Act of 2013 (HR 882), which would mandate tax compliance as a prerequisite for receiving a federal contract. The so-called "gang of eight" in the Senate is expected to release a comprehensive immigration reform package before the end of April which may require undocumented individuals to satisfy any unpaid federal tax liabilities as a prerequisite for citizenship.