

Tax policy in transition*

2009 Tax Legislative Outlook



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The heart of the matter

Change in Washington

The November 4 election was an important milestone for Democrats, giving them control of the White House and significantly increasing their majorities in both chambers of Congress. Now, attention has turned to the new President with a heightened expectation of change in the direction of the federal government.

Barack Obama will be sworn in as the 44th President of the United States on January 20. During the election campaign and since, President-elect Obama has demonstrated a disciplined, deliberative, and decisive management style, which will serve him well in facing the nation's challenges and overcoming obstacles to his agenda. In addition, he has assembled a strong team of experienced leaders to advise him and serve in his Administration.

With the presidency and strengthened majorities in Congress, Democrats once again will be firmly in control of the policy agenda in Washington. Democratic policy priorities are expected to refocus attention on domestic issues and additional funding for federal programs, with less emphasis on international issues.

Economic and tax policy agenda

The United States continues to face extraordinary fiscal and economic challenges from the continuing housing crisis, turmoil in financial markets, and the current economic recession. Recent economic indicators on GDP growth, job losses, and consumer anxiety suggest the U.S. economy will not rebound as quickly as thought just a few months ago. Indeed, the economic downturn appears to be deepening and spreading to more sectors.

As a result, action to accelerate economic recovery is the highest priority issue in Washington. Congressional leaders are actively working on economic recovery legislation with the expectation that the legislation will be passed by the new Congress and sent to the new President by mid-February. During the election campaign, President-elect Obama expressed support for a package of economic stimulus proposals, including individual tax relief, a business tax credit for new hires, increased small

business expensing, increased infrastructure spending, and relief to states. These proposals are likely to be part of any economic recovery solution.

Although economic recovery will be the primary focus of legislation in early 2009, President-elect Obama also campaigned on major legislative initiatives such as middle-income tax relief, business tax changes, healthcare reform, climate change, and energy independence. The new Administration is expected to include many of these domestic policy initiatives in its first budget submission to Congress, which will be released in February or March.

Congressional committee chairmen in both chambers will continue to exercise significant influence over the shaping of specific legislative proposals. For example, Senate Finance Committee Chairman Max Baucus (D-MT) already has staked out positions on economic recovery legislation and healthcare reform. House Ways and Means Committee Chairman Charles Rangel (D-NY) is preparing to reintroduce comprehensive tax reform legislation.

Federal budget considerations may act as a brake on the scope of tax and spending legislation. The federal deficit for fiscal 2009 is expected to exceed \$1 trillion. In addition, the United States faces near-term budget challenges, such as the scheduled expiration of individual tax relief enacted in 2001 and 2003, the growing number of individual alternative minimum tax (AMT) taxpayers, rising concern about global business competitiveness, and the growing cost of entitlement spending programs (Social Security, Medicare, and Medicaid).

While "pay-as-you-go" budget rules will be set aside initially for economic recovery legislation, as the economy recovers there is likely to be renewed concern about budget deficits and future tax legislation may require revenue offsets. For example, revenue-raising proposals may be considered in connection with legislation to renew business and individual tax provisions scheduled to expire after 2008 or 2009.

Impact of 2008 election

In the House of Representatives, Democrats gained 21 seats, with the result that there will be 257 Democrats and 178 Republicans. The expanded House majority may make it easier for Democratic leaders to manage the competing interests and diverse views of their party.

In the Senate, Democrats gained a minimum of seven seats. As of this writing, there will be 58 Democrats, including Senators Bernie Sanders (I-VT) and Joseph Lieberman (I-CT), and 41 Republicans in the Senate, with one race not final (Minnesota). Replacements are to be made for President-elect Obama (D-IL) and Vice President-elect Senator Joe Biden (D-DE), and for Senators Hillary Clinton (D-NY) and Ken Salazar (D-CO), who are resigning to join the Obama Administration as Secretary of State and Secretary of the Interior, respectively.

Although short of the 60 votes needed to prevent a filibuster, the increased Democratic majority in the Senate may make it more difficult for Republicans to block legislation they oppose, since on particular issues moderate Republicans may vote with Democrats.

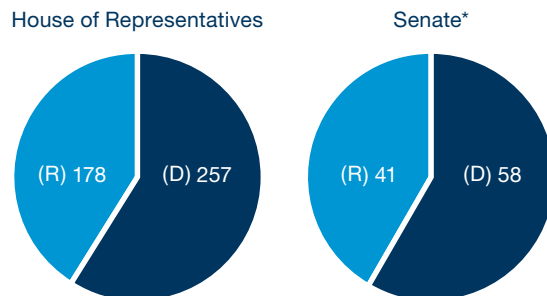
The Congressional budget process also could be used to overcome Republican opposition in the Senate to Democratic tax legislation.

At the same time, the 2008 elections continued a trend that began in the 2006 elections in which many of the newly elected Democratic Members of Congress come from states and Congressional districts traditionally held by Republicans. Many of these new Members from Republican-leaning regions of the country may hold more conservative views on tax and spending issues than the Administration or Congressional leaders, which could complicate Democratic efforts to govern. Congressional Republican leaders have indicated that they will work with the Obama Administration on some issues but oppose other proposals.

Both the House and Senate have a large class of incoming “freshmen” Representatives and Senators. This may make Congressional action more unpredictable and present a challenge to the leadership of both chambers and both parties in advancing their respective agendas.

There will be 36 U.S. Senate seats at stake in 2010—19 Republican and 17 Democratic—including six members of the Senate Finance Committee. (Four Republican Senators already have announced that they will not seek re-election; no Democratic Senators at this time have announced plans to retire.) Special elections will be held to fill out the terms of Senators Biden and Clinton.

Figure 1. 111th Congress balance of power



* Minnesota race remains subject to potential litigation; Democrats are expected to retain Illinois, Delaware, New York, and Colorado seats vacated by Senators Obama, Biden, Clinton, and Salazar.

Figure 2. New Senators in the 111th Congress

Mark Begich (D-AK)	Defeated incumbent Senator Ted Stevens (R)
Vacant (NY)	Senator Hillary Clinton (D) resigning to be Secretary of State
Kay Hagan (D-NC)	Defeated incumbent Senator Elizabeth Dole (R)
Mike Johanns (R-NE)	Succeeded retiring Senator Chuck Hagel (R)
Vacant (DE)	Senator Joe Biden (D) resigning to be Vice President
Jeff Merkley (D-OR)	Defeated incumbent Senator <i>Gordon Smith</i> (R)
Vacant (IL)	Senator Barack Obama (D) resigned to be President
James Risch (R-ID)	Succeeded retiring Senator Larry Craig (R)
Vacant (CO)	Senator Ken Salazar (D) resigning to be Interior Secretary
Jeanne Shaheen (D-NH)	Defeated incumbent Senator <i>John Sununu</i> (R)
Mark Udall (D-CO)	Succeeded retiring Senator Wayne Allard (R)
Tom Udall (D-NM)	Succeeded retiring Senator Pete Domenici (R)
Mark Warner (D-VA)	Succeeded retiring Senator John Warner (R)

Senate Finance Committee members in bold italics

Figure 3. Senate seats up in 2010

Democrats	Republicans	
Evan Bayh (D-IN)	Bob Bennett (R-UT)	Lisa Murkowski (R-AK)
Barbara Boxer (D-CA)	Kit Bond (R-MO)*	Richard Shelby (R-AL)
Chris Dodd (D-CT)	Sam Brownback (R-KS)*	Arlen Specter (R-PA)
Byron Dorgan (D-ND)	<i>Jim Bunning (R-KY)</i>	John Thune (R-SD)
Russ Feingold (D-WI)	Richard Burr (R-NC)	David Vitter (R-LA)
Daniel Inouye (D-HI)	Tom Coburn (R-OK)	George Voinovich (R-OH)*
Patrick Leahy (D-VT)	<i>Mike Crapo (R-ID)</i>	Open seat (CO)
<i>Blanche Lincoln (D-AR)</i>	Jim DeMint (R-SC)	Open seat (DE)**
Barbara Mikulski (D-MD)	<i>Charles Grassley (R-IA)</i>	Open seat (IL)
Patty Murray (D-WA)	Judd Gregg (R-NH)	Open seat (NY)**
Harry Reid (D-NV)	Johnny Isakson (R-GA)	
<i>Chuck Schumer (D-NY)</i>	Mel Martinez (R-FL)*	
<i>Ron Wyden (D-OR)</i>	John McCain (R-AZ)	

Senate Finance Committee Members in bold italics

* Retiring Member

** Special election

Tax policymakers

Obama Administration

Shortly after the November 4 election, President-elect Obama formed a transition team to begin organizing his Administration. Since then he has announced his entire Cabinet and numerous other Administration positions.

The key members of his economic team include Timothy Geithner as Treasury Secretary. Geithner currently is president of the Federal Reserve Bank of New York. President-elect Obama also announced former Treasury Secretary Lawrence Summers as director of the National Economic Council; former Congressional Budget Office (CBO) director Peter Orszag as director of the Office of Management and Budget (OMB); University of California, Berkeley economics professor Christina Romer as chair of the Council of Economic Advisers (CEA); and former congressional chief counsel Melody Barnes as director of the Domestic Policy Council.

President-elect Obama also announced the creation of a two-year, temporary Economic Recovery Advisory Board to advise him and his economic team on the design and implementation of an economic recovery plan. The board will be chaired by former Federal Reserve Chairman Paul Volcker. University of Chicago economics professor Austan Goolsbee will serve as staff director and chief

economist; Goolsbee also has been nominated as one of three CEA members. Additional board members will be announced.

Other key economic and tax policy officials to be named include Treasury Assistant Secretary for Tax Policy and IRS Chief Counsel. Don Korb has stepped down as IRS Chief Counsel, and Eric Solomon is expected to step down as Treasury Assistant Secretary for Tax Policy. As of this writing, Clarissa Potter is Acting IRS Chief Counsel. IRS Commissioner Doug Shulman is expected to continue for the remainder of his term.

Congressional leadership

There is general continuity in House and Senate leadership positions between the 110th and 111th Congresses. Nancy Pelosi (D-CA) continues as Speaker of the House, and Harry Reid (D-NV) continues as Senate Majority Leader. John Boehner (R-OH) and Mitch McConnell (R-KY) remain House and Senate Minority Leaders, respectively. Roy Blunt (R-MO) stepped down as House Minority Whip, resulting in some reshuffling of House GOP leadership positions. The tables on the next page lists the House and Senate leadership positions.

Figure 4. Key members of the Obama administration economic and tax policy team

Timothy Geithner	Treasury Secretary
Lawrence Summers	Director, National Economic Council
Peter Orszag	Director, Office of Management and Budget
Christina Romer	Chair, Council of Economic Advisers
Melody Barnes	Director, Domestic Policy Council
Paul Volcker	Chairman, Economic Recovery Advisory Board
Austan Goolsbee	Staff Director and Chief Economist, Economic Recovery Advisory Board; member, Council of Economic Advisers
To be named	Treasury Assistant Secretary for Tax Policy
Doug Shulman	IRS Commissioner
To be named	IRS Chief Counsel

Figure 5a. House leadership in the 111th Congress

Speaker of the House	Nancy Pelosi (D-CA)
Majority Leader	Steny Hoyer (D-MD)
Majority Whip	Jim Clyburn (D-SC)
Deputy Whip(s)	To be determined
Democratic Caucus Chair	John Larson (D-CT)
Democratic Caucus Vice Chair	Xavier Becerra (D-CA)
Democratic Campaign Committee Chair	Chris Van Hollen (D-MD)
Democratic Steering Committee Chair	George Miller (D-CA) and Rosa DeLauro (D-CT)
Minority Leader	John Boehner (R-OH)
Minority Whip	Eric Cantor (R-VA)
Deputy Minority Whip	Kevin McCarthy (R-CA)
Republican Conference Chair	Mike Pence (R-IN)
Republican Policy Committee Chair	Thaddeus McCotter (R-MI)
Republican Campaign Committee Chair	Pete Sessions (R-TX)

Figure 5b. Senate leadership in the 111th Congress

President of the Senate	Vice President-elect Joe Biden (D)
President pro tempore	Robert Byrd (D-WV)
Majority Leader	Harry Reid (D-NV)
Assistant Majority Leader	Richard Durbin (D-IL)
Democratic Conference Vice Chair	Charles Schumer (D-NY)
Democratic Senatorial Campaign Committee Chair	Bob Menendez (D-NJ)
Democratic Conference Secretary	Patty Murray (D-WA)
Democratic Policy Committee Chair	Byron Dorgan (D-ND)
Chief Deputy Whip	Barbara Boxer (D-CA)
Minority Leader	Mitch McConnell (R-KY)
Assistant Minority Leader	Jon Kyl (R-AZ)
Republican Conference Chair	Lamar Alexander (R-TN)
Republican Conference Vice Chair	John Thune (R-SD)
Republican Senatorial Campaign Committee Chair	John Cornyn (R-TX)

Congressional tax-writing committees

The 2008 election has resulted in changes to House and Senate committees. In the House, committee ratios have been adjusted to reflect the increased Democratic majority. Democratic vacancies have been filled, while Republican vacancies are expected to be filled in early January.

Meanwhile, with one race still undecided, decisions on committee ratios and assignments have been postponed in the Senate. Republicans are expected to lose committee seats as a result of the increased Democratic majority. There also will be changes in committee and subcommittee chairmanships as a result of new and departing Senators. For example, Senator John Kerry (D-MA) may take over for Senator Biden as Chairman of the Foreign Relations Committee, which has jurisdiction over tax treaties.

House Ways and Means Committee

Rep. Charles Rangel (D-NY) continues as chairman of the Ways and Means Committee and is expected to continue to promote comprehensive individual and business tax reform. Republicans elected Rep. Dave Camp (R-MI) to be ranking minority member on the committee, replacing Rep. Jim McCrery (R-LA), who retired. The Ways and Means Committee ratio has been adjusted to 26 Democrats and 15 Republicans, shifting two seats from Republicans to Democrats.

The new Democratic members are: Danny Davis (D-IL), Bob Etheridge (D-NC), John Yarmuth (D-KY), Brian Higgins (D-NY), and Linda Sanchez (D-CA). The new Republican members are Ginny Brown-Waite (R-FL); Geoff Davis (R-KY); Dave Reichert (R-WA); Charles Boustany (R-LA); Dean Heller (R-NV); and Peter Roskam (R-IL). There may be changes in Subcommittee ranking members with the elevation of Rep. Camp to full Committee ranking member. Rep. Camp previously was ranking minority member of the Subcommittee on Health.

Following is a table of Ways and Means Committee members in the 111th Congress.

Figure 6. House Ways and Means Committee membership, 111th Congress

Democrats	Republicans
Charles Rangel (D-NY), chairman	Dave Camp (R-MI), ranking minority member
Pete Stark (D-CA)	Wally Herger (R-CA)
Sander Levin (D-MI)	Sam Johnson (R-TX)
Jim McDermott (D-WA)	Kevin Brady (R-TX)
John Lewis (D-GA)	Paul Ryan (R-WI)
Richard Neal (D-MA)	Eric Cantor (R-VA)
John Tanner (D-TN)	John Linder (R-GA)
Xavier Becerra (D-CA)	Devin Nunes (R-CA)
Lloyd Doggett (D-TX)	Patrick Tiberi (R-OH)
Earl Pomeroy (D-ND)	Ginny Brown-Waite (R-FL)
Mike Thompson (D-CA)	Geoff Davis (R-KY)
John Larson (D-CT)	Dave Reichert (R-WA)
Earl Blumenauer (D-OR)	Charles Boustany (R-LA)
Ron Kind (D-WI)	Dean Heller (R-NV)
Bill Pascrell (D-NJ)	Peter Roskam (R-IL)
Shelley Berkley (D-NV)	
Joseph Crowley (D-NY)	
Chris Van Hollen (D-MD)	
Kendrick Meek (D-FL)	
Allyson Schwartz (D-PA)	
Artur Davis (D-AL)	
Danny Davis (D-IL)	
Bob Etheridge (D-NC)	
John Yarmuth (D-KY)	
Brian Higgins (D-NY)	
Linda Sanchez (D-CA)	

Senate Finance Committee

Senator Max Baucus (D-MT) continues as chairman and Senator Charles Grassley (R-IA) continues as ranking minority member of the Senate Finance Committee. Chairman Baucus is expected to focus on healthcare reform and international tax issues, while Senator Grassley is likely to continue to focus on issues he pursued last year, including executive compensation, Medicare, and tax-exempt organizations.

The committee ratio has not been determined; however, Republicans are expected to lose at least one seat. With Senator Salazar resigning to become Interior Secretary, there will be at least one Democratic vacancy. Following is a table of Finance Committee members in the 111th Congress.

Figure 7. Senate Finance Committee members, 111th Congress

Democrats	Republicans
Max Baucus (D-MT), chairman	Charles Grassley (R-IA), ranking minority member
John Rockefeller (D-WV)	Orrin Hatch (R-UT)
Kent Conrad (D-ND)	Olympia Snowe (R-ME)
Jeff Bingaman (D-NM)	Jon Kyl (R-AZ)
John Kerry (D-MA)	Jim Bunning (R-KY)
Blanche Lincoln (D-AR)	Mike Crapo (R-ID)
Ron Wyden (D-OR)	Pat Roberts (R-KS)
Charles Schumer (D-NY)	John Ensign (R-NV)
Debbie Stabenow (D-MI)	Open seat or seats
Maria Cantwell (D-WA)	
Open seat	

Congressional schedule

The 111th Congress convened on January 3, and new Members were sworn in on January 6. President-elect Obama and Vice President-elect Biden assume office on January 20.

With a new Administration, the legislative year typically would be expected to get off to a slow start. However, in light of the current economic crisis and at the urging of President-elect Obama, Congress is expected to take action beginning in January. Congressional leaders want to send an economic recovery bill to the White House by mid-February.

The statutory deadline for the Administration's budget submission is the first Monday in February, i.e., February 2. (Neither President Bill Clinton nor President George W. Bush submitted a complete budget by that date in their first year in office.) By the start of the Easter recess period, Congress typically adopts a "budget resolution" setting overall spending and revenue targets for the next fiscal year (fiscal year 2010). Meanwhile, a "continuing resolution" funding current-year (fiscal year 2009) government operations is scheduled to expire on March 6. Congress will need either to complete the fiscal year 2009 appropriations process or to pass a further continuing resolution by that date.

Figure 8. 2009 Congressional schedule

House and Senate convene	January 3
New member swearing-in	January 6
Inauguration Day	January 20
President's State of the Union address	Date to be announced
President's Day recess	February 16–23
"Continuing resolution" expires	March 6
Easter recess	April 6–21
Statutory budget resolution deadline	April 15
Memorial Day recess	May 25–June 2
Independence Day recess	June 29–July 7
August recess	August 3–September 8
Fiscal Year 2010 begins	October 1
Target adjournment	October 30

Economic recovery legislation

Current economic situation

In December, the National Bureau of Economic Research, the private research organization responsible for identifying recessions, announced that the current recession began in December 2007. At 13 months and counting, the current recession already has surpassed the average postwar recession duration of approximately 11 months. Projections from various forecasters expect the current recession to last between 18 and 24 months.

Stronger economic growth over the past year helped prevent a greater drop in economic activity. The relative strength of the world economy and the weakness of the dollar earlier in the year helped promote U.S. exports. However, as economic weakness has spread globally, growth in demand for U.S. exports has fallen off.

Figure 9 below compares the length and the cumulative decline in employment over recessions for the post-war period. During the 1957–1958 recession, employment fell by four percent. In the current recession, employment has fallen by 1.4 percent through November 2008.

Figure 9. Length of post-war recessions in months, with cumulative drop in employment over recession

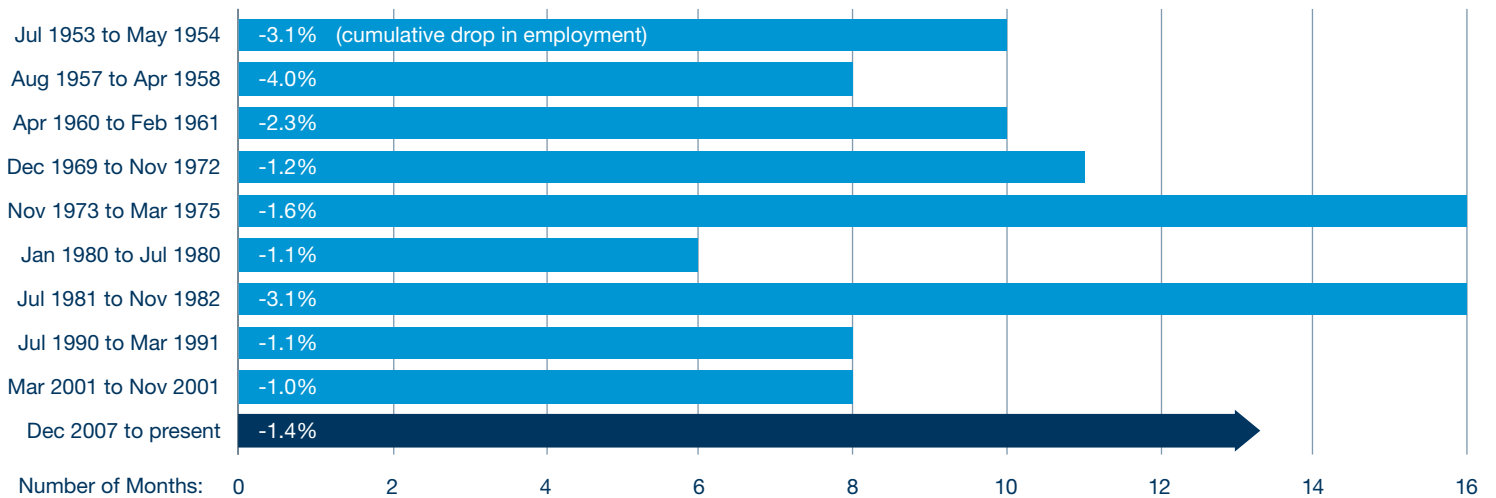


Figure 10. Percentage change in real GDP, 2004–2009

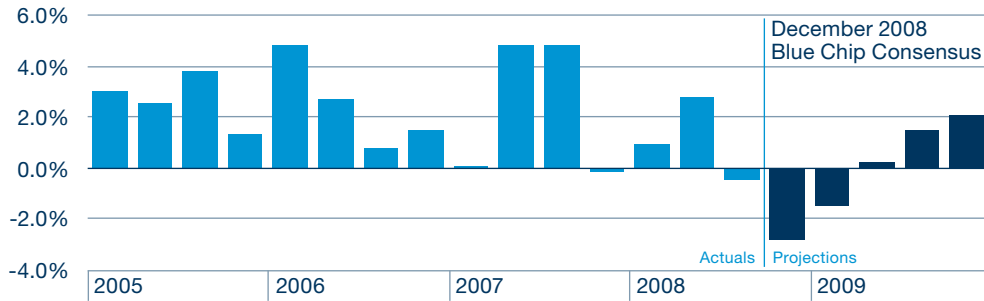


Figure 11a. Non-farm employment, 2004–2008 (millions)

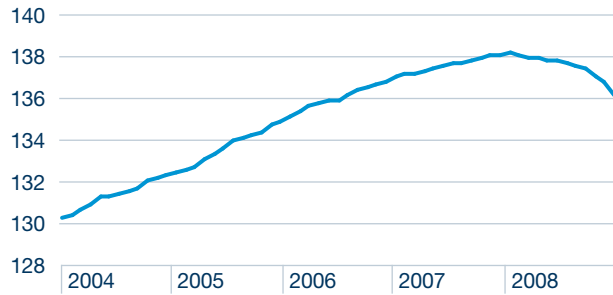
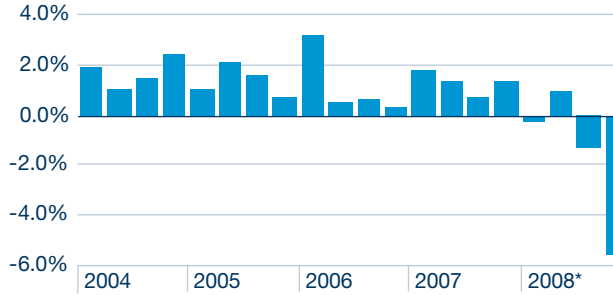
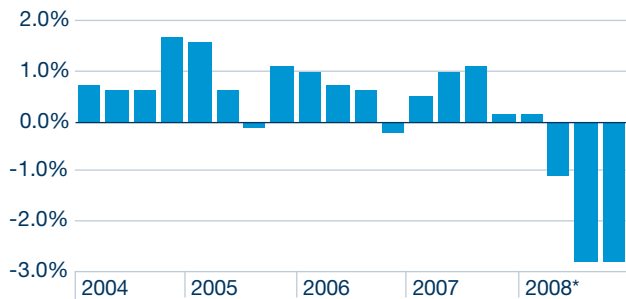


Figure 11b. Percentage change in quarterly retail sales, 2004–2008



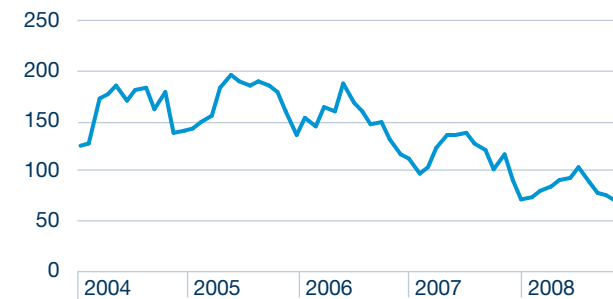
*Fourth quarter 2008 is estimated based on Oct. and Nov. sales.

Figure 11c. Percentage change in quarterly industrial production, 2004–2008



*Fourth quarter 2008 is estimated based on Oct. and Nov. values.

Figure 11d. Housing starts 2004–2008 (thousands)



Source: Federal Reserve, U.S. Census Bureau, U.S. Bureau of Labor Statistics, and PricewaterhouseCoopers calculations.

The December 2008 Blue Chip consensus expects that GDP will fall in the fourth quarter of 2008 and the first quarter of 2009, that the second quarter essentially will be flat, and that the third quarter and beyond will experience a growing economy (see Figure 10).

Most measures of economic activity deteriorated throughout 2008:

- Nonfarm payrolls peaked in December 2007, with 1.9 million jobs lost through November 2008 (see Figure 11a).
- Retail sales have fallen at an accelerating rate over the last five months. November 2008 sales were over seven percent lower than November 2007. Sales in the fourth quarter of 2008, which included the holiday shopping season, could be almost six percent lower than sales in the third quarter (see Figure 11b).
- Industrial production fell in the second and third quarters of 2008 and is expected to fall in the fourth quarter (see Figure 11c). The decline over these quarters has been the largest since the 1990-91 recession.
- Housing starts have declined in 2007 and 2008. The number of housing starts in the summer, the peak of the building season, was half as large in 2008 in comparison with 2004 through 2006 (see Figure 11d).

The current recession in the real economy is at least partially attributable to continued turmoil in financial markets. Banks continue to be reluctant to lend and are demanding premiums to compensate for perceived risks. Based on the latest information from the Federal Reserve, commercial credit increased at its lowest rate since the 1990-91 recession.

The federal government has acted on several fronts to confront the weak economy. The federal government's Troubled Asset Relief Program (TARP) is attempting to reinforce lenders and provide new confidence through \$700 billion of capital injections and loans. At the same time, the Federal Reserve has eased interest rates from 4.25 percent at the beginning of 2008 to between zero and 0.25 percent in December. The Federal Reserve also has boosted lending through several new funding mechanisms, including its term auction facility, a commercial paper funding facility, and money market asset-backed commercial paper and other money market securities funding facilities. As a result, the Federal Reserve balance sheet has increased to over \$2.2 trillion in December from around \$950 billion in September.

The combined impact of increased federal spending and slower revenue collections attributable to the economic slowdown has led to an increase in the federal budget deficit.

Fiscal year 2008 results

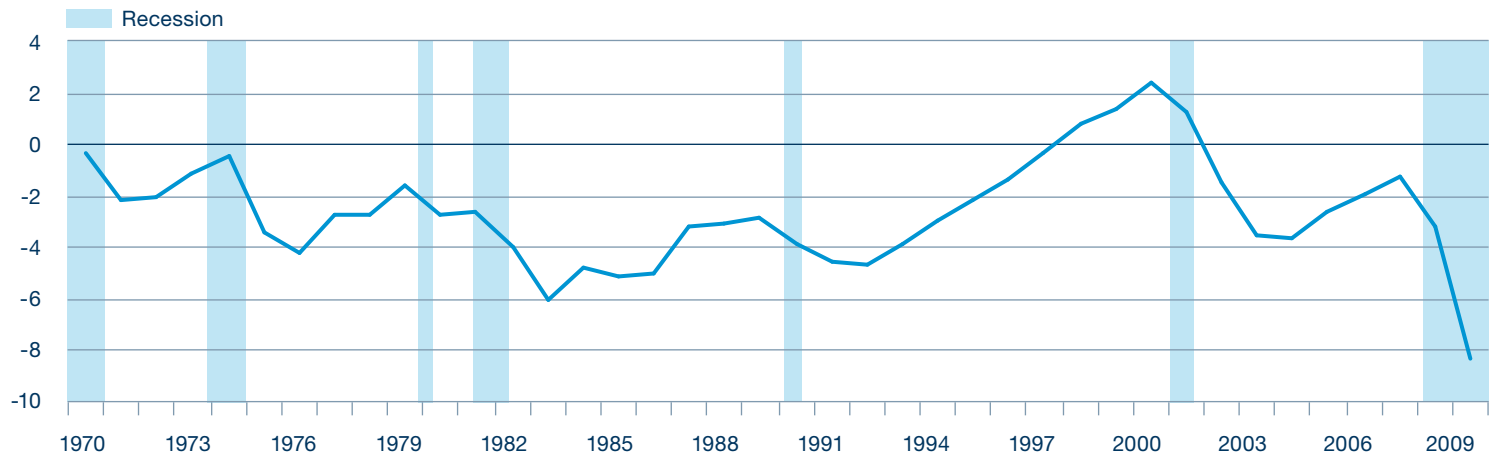
The deficit for the fiscal year ended September 30, 2008, reached \$455 billion, \$293 billion greater than the fiscal year 2007 deficit and \$236 billion greater than the fiscal 2008 levels projected in January 2008. The increased federal budget deficit is attributable to the economic recession, stimulus legislation in early 2008, and increased defense spending. As a share of GDP, the 2008 budget deficit amounted to 3.2 percent, one-third larger than the average over the last 40 years of 2.4 percent.

Fiscal year 2009 and beyond

The budget outlook for fiscal year 2009, which began in October, appears even worse. On January 7, 2009, the Congressional Budget Office (CBO) released its most recent economic and budget outlook for the 2009–2019 period.

CBO estimated that the budget deficit would reach \$1.2 trillion in 2009. That figure includes the budgetary impact of the TARP legislation (which also extended certain expiring tax provisions) and the current recession, but does not reflect additional economic recovery legislation expected to be enacted this year. Even without taking into account such legislation, CBO estimates that the federal budget deficit in 2009 will reach 8.3 percent of GDP, a level not reached since World War II.

Figure 12. Federal budget deficit as a share of GDP, FY 1970-2009



Source: CBO

Assuming the new economic recovery legislation increased the deficit by \$500 billion in 2009 (with additional amounts in 2010), the deficit would exceed 12 percent of GDP in 2009.

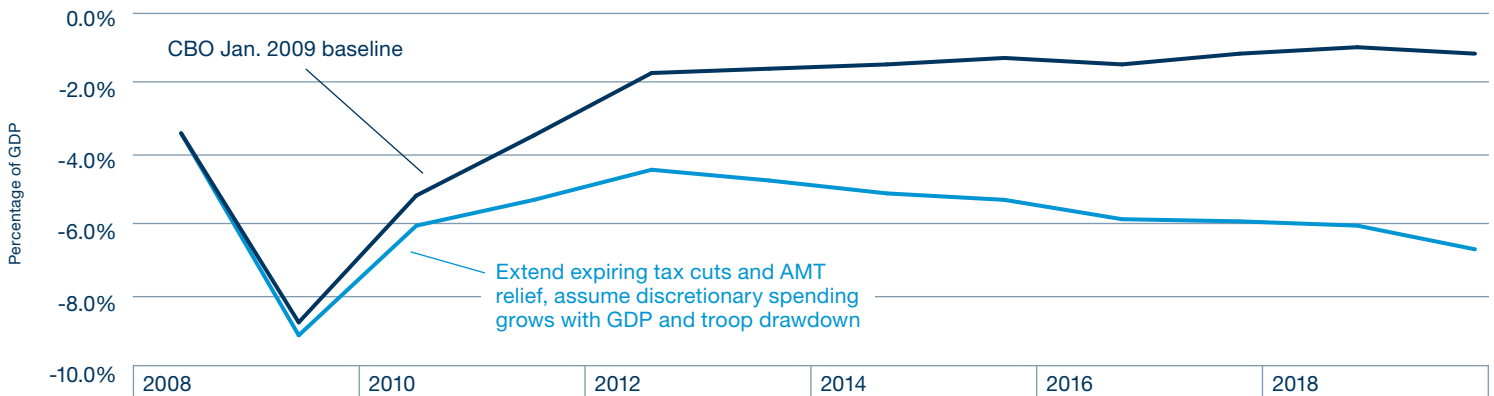
Beyond 2009, CBO projects the budget deficit by reference to current law. As required by congressional scorekeeping rules, CBO's projection assumes the expiration of the 2001–2003 tax cuts, slow growth in discretionary spending, and a continuation of the Iraq and Afghanistan conflicts.

To provide an alternative view of the deficit situation, CBO also furnished a projection under which it assumes all of the following: extension of all individual tax provisions

scheduled to sunset after 2010; indexation of the individual AMT for inflation; extension of miscellaneous annual expiring tax provisions; higher spending by assuming that future discretionary spending increases with the size of the economy rather than being held fixed in real terms; and a reduction in spending through troop reductions in Iraq and Afghanistan (reducing the number of troops to 30,000 by 2011). Figure 13 demonstrates the 10-year deficit outlook under these projections.

Under the alternative assumption, the deficit will exceed six percent of GDP toward the end of the 10-year projection period, well above the 40-year average ratio of 2.4 percent.

Figure 13. Federal Budget Deficit Projections (Percentage of GDP, CBO January 2009 Projections)



Source: CBO and PricewaterhouseCoopers calculations.

Economic recovery proposals

The new Congress is expected to consider a major economic stimulus package as its initial priority, with the goal of sending a bill to the White House by mid-February. President-elect Obama has directed his economic team to develop recommendations for an economic recovery package in consultation with Congress.

President-elect Obama has said the package will include infrastructure spending and energy independence projects. Democratic leaders also have expressed support for aid to state and local governments as well as federal nutrition assistance. Congress last year passed an extension of unemployment benefits and pension funding relief.

Although the focus may be on spending programs, the economic stimulus bill also may include tax relief. During the election campaign, President-elect Obama proposed a \$500 (\$1,000 for couples) refundable tax credit for individuals, a business tax credit for new hires, enhanced small business expensing, tax-free unemployment benefits, and relaxed rules on IRA and 401(k) withdrawals.

Other economic stimulus tax proposals under discussion include extension of “bonus” depreciation, expansion of the net operating loss (NOL) carryback period, and enhancement of existing renewable energy tax incentives. There also are proposals to extend expiring tax provisions, including the research tax credit, and enhance the ability of companies to access foreign earnings in response to the current economic crisis.

The cost of an economic recovery package could exceed \$750 billion over the next several years. The net impact of these provisions on the deficit, and more importantly on economic growth, would depend on their ability to encourage additional economic activity and the response of financial markets to the significant increase in federal debt.

Drivers of tax legislation

The U.S. tax system faces significant challenges over the next several years. In the absence of legislative action, individual income tax cuts enacted as part of the 2001 and 2003 tax acts will expire, and a growing number of individuals will become subject to the AMT. There is a growing belief that these issues can be addressed on a permanent basis only in the context of fundamental tax reform.

While tax relief for individuals may drive tax reform, Congress also may consider business tax reforms to promote U.S. investment and employment. The U.S. economy today is more globally integrated than ever, both through exports and cross-border investment. The ability of U.S. companies to grow and compete in the foreign markets that represent 95 percent of the world's consumers is essential to future U.S. economic growth. There is growing concern that differences between the U.S. tax system and the tax laws of the country's major trading partners adversely affect the international competitiveness of U.S. businesses.

2010 sunset of tax relief for individuals

The scheduled expiration after 2010 of key tax cuts enacted in 2001 and 2003 is a central reason why many policymakers view tax reform as inevitable. Unless new legislation is enacted, the individual tax code largely would revert to its pre-2001 status beginning in 2011. More than 116 million individual taxpayers would be affected by the scheduled termination of tax relief after 2010, with the result that federal taxes would grow by nearly \$3 trillion over the next decade.

More specifically, unless Congress acts:

- The current individual ordinary income tax schedule would revert to the pre-2001 rates, resulting in higher tax rates for most taxpayers beginning in 2011. The 10-percent bracket for low-income taxpayers would revert to 15 percent; a portion of the 15-percent bracket for married couples filing joint returns would be taxed at 28 percent; and other brackets would increase, with the top tax rate reaching 39.6 percent.
- The current capital gains tax rates of zero and 15 percent would revert to 10 and 20 percent, respectively.
- Dividends—currently taxed at zero and 15 percent—would be taxed as ordinary income and therefore would be subject to a top rate of 39.6 percent.
- The estate tax, which is to be eliminated in 2010, would return in 2011 with a 55-percent top rate and a \$1 million exemption.
- The increased \$1,000 child tax credit would be halved, the increased standard deduction providing tax relief for married filers would decline by more than 15 percent, and many education tax incentives would expire after 2010.

Expanded reach of individual AMT

The considerable cost of individual AMT reform is viewed as the second motivating factor for tax reform. Congress has not yet found a permanent solution to the expanding reach of the individual AMT.

Once intended to prevent high-income individuals from using tax preferences to avoid paying any tax, the AMT increasingly has operated as a tax on middle-income families. Unlike the tax brackets and personal exemptions under the regular income tax, the AMT is not adjusted for inflation.

As a result, over time, an increasing number of individual taxpayers have become subject to AMT simply because they claim personal exemptions, the standard deduction, or deductions for state and local taxes. The 2001 and 2003 tax cuts would have further increased the number of AMT taxpayers if not for the temporary increases in the AMT exemption that have been enacted since 2001—the so-called “AMT patch.”

Without action by Congress, the number of AMT taxpayers will increase dramatically. In fact, AMT taxpayers would rise to 28 million in 2009 from four million in 2008 unless Congress enacts another “patch”

this year. (Figure 14 shows the estimated percentage of individual taxpayers subject to AMT in 2010 by income, assuming there is no “patch” in effect for that year.) By 2018, assuming extension of the 2001 and 2003 tax reductions after 2010 and no AMT relief, AMT taxpayers would increase to approximately 55 million, or roughly half of all taxpayers with positive income tax liability.

If the 2001 and 2003 tax cuts are extended after 2010, permanently extending the “AMT patch” and indexing the AMT for inflation are estimated to increase the deficit by \$1.6 trillion over 10 years (2009–2018). Given this substantial cost of relief, there appears to be broad agreement that the AMT issue can be addressed on a permanent basis only as part of tax reform legislation.

Figure 14. Percentage of taxpayers on AMT, assuming no “patch” in 2010

AGI	2006	2010
Less than \$20,000	0.0%	0.0%
\$20,000–\$40,000	0.0%	0.6%
\$40,000–\$50,000	0.2%	5.5%
\$50,000–\$75,000	0.5%	17.4%
\$75,000–\$100,000	1.6%	52.9%
\$100,000–\$200,000	10.2%	85.6%
\$200,000–\$500,000	74.0%	98.1%
\$500,000–\$1 million	47.3%	70.9%
Over \$1 million	23.1%	31.5%
Total	2.5%	17.9%

Source: Joint Committee on Taxation (2007)

International business competition

The desire of policymakers for an internationally competitive business tax system reflects the increasing integration of the United States in the global economy. Low-cost communications and transportation have expanded the ability of corporations to operate on a global scale, both through trade and cross-border investment. Over the past 40 years, U.S. exports have doubled relative to the size of the economy, while the share of corporate profits earned abroad by U.S. corporations has more than tripled.

At the same time, the United States, which once dominated the ranks of the leading international companies, now is one competitor among many. Worldwide, cross-border investment expanded from less than six percent of worldwide output in 1980 to 26 percent in 2006. In 1960, the United States accounted for more than half of outward cross-border investments; by 2006, it accounted for less than one-fifth. In 1960, the United States was home to 70 of the top 100 industrial corporations; now it is home to 38.

The question facing U.S. policymakers is how tax policy should respond to the changing patterns of foreign investment since the early 1960s. Two key issues receiving attention are the U.S. corporate tax rate and the tax rules applicable to foreign earnings of U.S. companies.

Corporate tax rates. The U.S. statutory corporate tax rate is much higher than the rates of most of its trading partners. The combined top federal, state, and local U.S. corporate income tax rate is 39.3 percent—the federal rate of 35 percent plus an average state and local tax rate of 6.54 percent (4.3 percent after deduction against federal income tax). This is the second highest (after Japan) among the 30 members of the Organization for Economic Cooperation and Development (OECD) and 12.7 percentage points greater than the OECD average (see Figure 15).

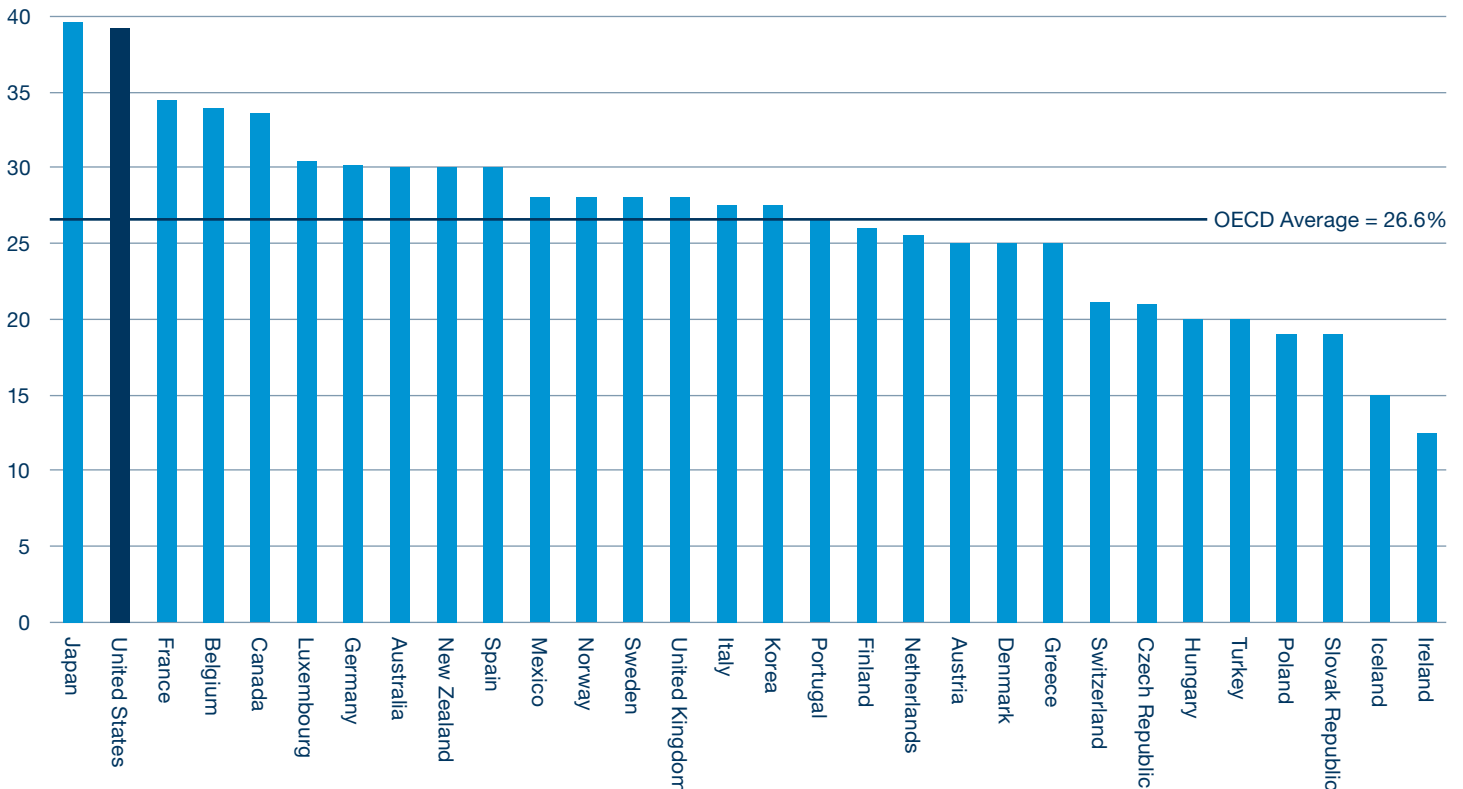
U.S. taxes on foreign income. For many U.S. companies, another key issue for maintaining competitiveness abroad is the ability to defer U.S. tax on active foreign earnings until this income is brought home. Approximately one-third of OECD countries provide for such worldwide taxation. The remaining two-thirds have “territorial” tax systems, under which active foreign earnings are not taxed at all by the home country. Enacting further limitations on the ability of U.S. companies to defer U.S. tax on foreign earnings could erode the competitiveness of U.S. companies.

Impact of federal budget outlook on tax reform

Projected federal budget deficits are expected to create pressure for tax reform to be “revenue neutral,” meaning that tax cuts would have to be offset by tax increases. For example, the Tax Reform Act of 1986, which may be seen as a precedent for future tax reform, reduced individual and corporate tax rates on a revenue-neutral basis by broadening the tax base and eliminating certain individual and business tax preferences.

The Tax Reform Act of 1986 was also projected to shift \$120 billion in taxes onto corporations to fund individual tax relief in the first five years following enactment. As a result, even if tax reform is revenue-neutral overall, business taxes could increase to pay for some of the cost of individual tax relief. In addition, there could be shifts in tax burdens within the business sector.

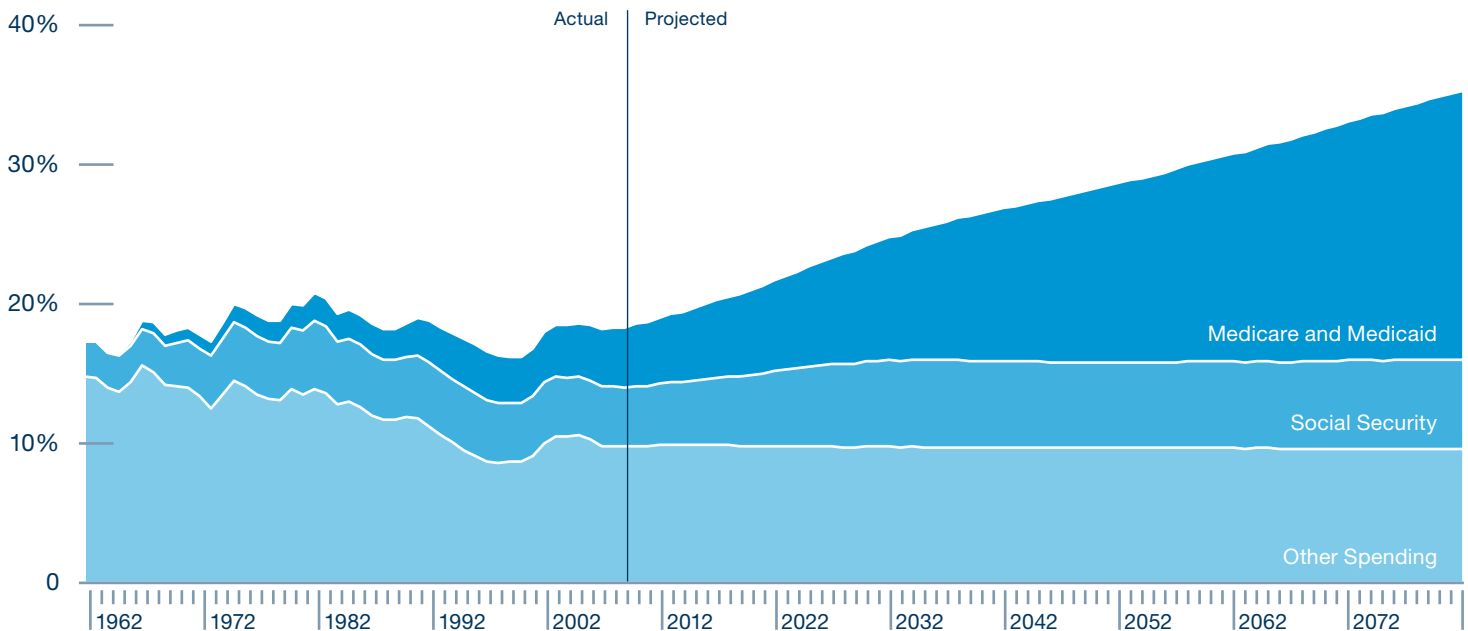
Figure 15. 2008 corporate tax rates, OECD countries



Impact of long-term fiscal challenges on tax reform

Projected increases in spending on Social Security, Medicare, and Medicaid in coming decades (see Figure 16 below) will require reforms to hold down the rate of growth of these programs and possibly higher future taxes. By 2050, CBO projects combined spending on these three programs to exceed 18 percent of GDP, up from about eight percent in 2007. To put this long-term spending projection in perspective, total federal revenue from all sources, including individual, corporate, payroll, and excise taxes, has averaged 18.3 percent of GDP over the past 40 years.

Figure 16. Long-term projection of federal spending (excluding debt service), as share of GDP



Source: Congressional Budget Office (December 2007)

Tax reform proposals

In light of the preceding factors, numerous tax reform proposals have attracted attention in recent years. Among these, a comprehensive tax reform bill introduced in October 2007 by Ways and Means Chairman Rangel is analyzed below; Treasury base-broadening options from December 2007 also are noted. Figure 18 (pages 22–24 of this report) outlines President-elect Obama’s campaign tax plan, which includes international tax restructuring proposals.

Chairman Rangel’s tax reform legislation

In October 2007, Ways and Means Chairman Rangel introduced a comprehensive tax reform bill (H.R. 3970, the Tax Reduction and Reform Act of 2007) that would repeal the individual AMT and reduce the corporate income tax rate from 35 percent to 30.5 percent. H.R. 3970 is revenue-neutral, with revenue loss from individual AMT repeal fully offset by individual tax increases, and revenue loss from corporate rate reduction offset by business tax increases (see Figure 17 on page 20).

Three corporate revenue-raising provisions account for most of the offsets proposed to pay for rate reduction. These are proposals to repeal the domestic manufacturing deduction, repeal the “last-in, first-out” (LIFO) accounting method, and a measure to defer deductions allocable to foreign-source income and restrict the use of foreign tax credits. That last proposal has generated considerable concern within the business community.

This year, Chairman Rangel is expected to propose a revised version of his comprehensive tax reform bill. Among other changes, Chairman Rangel is expected to propose reducing the corporate income tax rate to 28 percent. If so, the bill could include other business tax increases, such as additional limitations on accelerated depreciation, to offset the additional revenue loss associated with the anticipated further reduction in the corporate tax rate.

Bush Treasury base-broadening options

The U.S. Treasury Department under President George W. Bush also has contributed to the tax reform debate by releasing a December 2007 report on U.S. business competitiveness. Although it does not make specific recommendations, the report discusses three approaches to comprehensive business income tax reform on a revenue-neutral basis:

- A broad business tax base and a business tax rate of 28 percent with slower cost recovery (or 31 percent if accelerated depreciation were maintained).
- A broad business tax base maintaining current tax rates combined with 35-percent partial expensing for equipment, structures, and inventories.
- Replacement of all business taxes with a “business activities tax” (i.e., a value-added tax) imposed at a rate of five to six percent.

Among other changes, the broad business tax base options would repeal the domestic manufacturing deduction and would not extend the research tax credit.

Figure 17. Chairman Rangel's 2007 Tax Reform Bill (H.R. 3970, 110th Congress)

Individual income tax provisions	10-year revenue effect (2008-17)
Repeal individual alternative minimum tax	(\$796 billion)
Modify UBIT rules for certain investment partnerships	(\$1 billion)
Increase standard deduction	(\$48 billion)
Expand earned income tax credit	(\$29 billion)
Increase refundable child tax credit	(\$9 billion)
Impose 4% surtax on income over \$200K and 4.6% over \$500K	\$832 billion
Restore Pease and PEP	\$29 billion
Tax carried interest as ordinary income	\$26 billion
Tax offshore nonqualified deferred compensation*	\$23 billion
Clarify self-employment tax on S corporations and partnerships	\$9 billion
Modify 2% floor on miscellaneous itemized deductions	\$7 billion
Require reporting by brokers on sales of stocks*	\$4 billion
Tax certain gain on related-person sales as ordinary income	\$0.1 billion
Corporate income tax provisions	
Reduce corporate income tax rate from 35% to 30.5%	(\$365 billion)
Permanent extension of enhanced small business expensing	(\$21 billion)
Repeal domestic manufacturing deduction	\$115 billion
Repeal "last-in, first-out" (LIFO) method of accounting	\$107 billion
Defer expenses on foreign income and limit foreign tax credits	\$106 billion
Repeal worldwide interest expense allocation	\$26 billion
Increase goodwill amortization period from 15 to 20 years	\$21 billion
Repeal lower of cost or market method of accounting	\$7 billion
Limit eligibility for tax treaty benefits	\$6 billion
Reduce dividends received deduction	\$5 billion
Codify economic substance judicial doctrine	\$4 billion
Terminate domestic international sales corporation provisions	\$0.9 billion
Income on exercise of stock option in S corporation with ESOP	\$0.6 billion
Clarify gain recognized in certain spin-off transactions	\$0.2 billion
Repeal nonaccrual experience method for C corporations	\$0.2 billion

* Provision enacted into law as part of subsequent tax legislation

Potential revenue raisers

For purposes of economic recovery legislation, Congressional “pay-as-you-go” budget rules—requiring any tax cuts to be completely offset with either tax increases or reductions in mandatory (entitlements) spending—are not expected to apply. However, as the economy begins to recover, there may be renewed focus on the need to control federal budget deficits. As a result, there likely will be pressure to consider business tax increases and other revenue-raising tax proposals to offset future tax legislation.

In addition to general proposals relating to deferral and “tax havens,” President-elect Obama’s campaign tax plan includes specific revenue-raising tax provisions, such as codification of the economic substance judicial doctrine and taxation of “carried interest” received by hedge fund and private equity managers as ordinary income rather than capital gain. He also has proposed closing a “CEO pay deductibility loophole.”

The Administration’s budget submission could provide additional details regarding President-elect Obama’s campaign tax proposals and also could include additional revenue-raising tax proposals. For example, President-elect Obama has expressed support for closing the “tax gap”—the difference between what taxpayers owe and the amount they actually pay. The tax gap previously has been estimated by the IRS to be \$345 billion. Prior tax gap proposals have focused on increased information reporting and withholding.

Congress has considered a number of revenue-raising proposals in recent years that were not enacted and hence remain available for potential use as offsets. In addition, the tax reform bill proposed by House Ways and Means Committee Chairman Rangel (discussed above) contains a number of revenue-raising provisions. Some of the revenue raisers proposed in 2007 by Chairman Rangel already have been enacted.

Other potential sources of revenue that might be considered include past Administration budget proposals, as well as recent or pending reports and investigations on particular tax issues. The Joint Committee on Taxation staff has been conducting a review of transfer pricing rules, and a long-overdue Treasury report on corporate inversion is still pending.

The Senate Finance Committee is expected to focus this year on a variety of international tax issues, including transfer pricing, cost sharing, earnings stripping, and deferral. Last year, the committee released draft legislation on foreign reinsurance and held hearings on “tax havens.” In addition, Finance Committee Ranking Member Grassley is expected to continue to focus on tax-exempt issues, including nonprofit hospitals and colleges and universities.

Separately, the Senate Permanent Subcommittee on Investigations has sent a questionnaire to certain U.S. businesses requesting detailed information on aspects of the company’s income tax posture; the subcommittee is expected to issue a report that may suggest tax law changes. The subcommittee also recently released reports on the use of derivatives to avoid foreign withholding on dividends, and U.S. tax evasion involving offshore banks.

The House Ways and Means Committee has been examining the tax treatment of derivatives and foreign reinsurance.

For a list of potential revenue-raising tax provisions proposed in past bills, Administration budgets, or CBO or JCT staff reports, see the Appendix at the end of this report.

President-elect Obama's campaign tax plan

During the election campaign, President-elect Obama proposed permanent extension of the 2001 and 2003 tax cuts for most individuals, while proposing increasing taxes on individuals with income above \$250,000 by restoring the pre-2001 tax law for those taxpayers. His proposals include raising the top individual income tax rate to 39.6 percent (from 35 percent) and increasing the capital gain and dividend tax rate for such individuals to 20 percent (from 15 percent). In addition, President-elect Obama has proposed maintaining the estate tax at the levels scheduled for 2009.

On business taxes, President-elect Obama has proposed restructuring U.S. international tax rules to address provisions that “reward corporations that retain their earnings overseas” and that encourage companies to “ship jobs overseas.” Although details have not been provided, campaign advisers have said that he is proposing to limit rather than repeal deferral. President-elect Obama also has proposed addressing offshore tax havens. Under the campaign proposal, the resulting revenue would be used to lower corporate tax rates for companies that “expand or start operations in the United States.”

Figure 18. Obama Election Campaign Tax Plan

I. Economic crisis proposals	
1. Retirement savings	Allow penalty-free hardship withdrawals from IRAs and 401(k) accounts of 15 percent, up to \$10,000, in 2008 (retroactive) and 2009. Instruct Treasury to suspend required withdrawals for seniors over age 70-1/2. Exempt any withdrawals made up to the required minimum amount from taxation.
2. Unemployment insurance benefits	Extend unemployment benefits and temporarily eliminate taxes on benefits received.
3. Business provisions	Create refundable American Jobs Tax Credit of \$3,000 for each additional full-time employee hired by an existing business in 2009 and 2010. Increase section 179 small business investment expensing limit to \$250,000 through the end of 2009. Under current law, the limitation is \$250,000 for 2008 and \$125,000 in 2009.
4. Tax rebates	Accelerate effects of proposed 2009 tax relief by providing tax rebate checks (\$500 for individuals; \$1,000 for families).
II. Business proposals	
1. Corporate tax rate	Support “Patriot Employer Act” (S. 1945), which would provide a tax credit equal to one percent of taxable income to businesses that meet certain requirements (e.g., pay at least 60 percent of employee health care premiums, maintain or increase U.S. workforce relative to foreign workers, and offer retirement savings plan with matching contributions).
2. International tax	Address tax provisions that “reward corporations that retain their earnings overseas.” Address offshore “tax havens.” Create international “tax evasion” watch list and penalize companies that report income from offshore tax havens on list.
3. Research credit	Make permanent.
4. Oil and gas industry	Eliminate certain tax provisions, including special expensing rules, foreign tax credit, and domestic manufacturing deduction. Impose windfall profits tax on oil when price exceeds \$80 per barrel.

5. Renewable energy and energy efficiency	<p>Extend the credit for producing electricity from renewable sources for five years.</p> <p>Provide retooling tax credits for domestic auto plants and parts manufacturers to build new fuel-efficient vehicles.</p> <p>Provide 30-percent tax credit for cost of installing E85 ethanol refueling pumps.</p> <p>Eliminate the 60,000 per-manufacturer cap on tax credits for the purchase of fuel-efficient vehicles.</p> <p>Provide tax incentives for cellulosic ethanol.</p> <p>Expand tax credit for biofuel refineries.</p> <p>Equalize the tax treatment of employer-provided parking and commuting benefits (e.g., transit, carpooling, and vanpooling).</p> <p>Extend existing consumer tax credits for energy efficient appliances and products.</p> <p>Provide a \$7,000 tax credit for the purchase of advanced technology vehicles</p>
6. Telecommunications	Provide tax incentives for deployment of next-generation broadband.
7. Revenue offsets	<p>Tax carried interest of hedge funds and partnerships as ordinary income.</p> <p>Codify economic substance doctrine.</p> <p>Reduce the “tax gap” (i.e., the difference between what taxpayers owe and what is actually paid).</p> <p>Close the “CEO pay deductibility loophole.”</p>
III. Individual proposals	
1. Top individual rate	39.6 percent.
2. Dividends and capital gains	<p>Increase rates to 20 percent for income over \$250,000 (\$200,000 for single returns).</p> <p>Preserve current rates on income below these income thresholds.</p> <p>Eliminate capital gains taxation of start-up businesses.</p>
3. Estate tax	Freeze the estate tax at 2009 level (i.e., \$3.5 million per-person exemption and 45-percent top rate).
4. Other 2001/2003 tax cuts	<p>Restore phaseouts of personal exemptions and itemized deductions for high-income taxpayers.</p> <p>Extend rate cuts on the lower four brackets (income up to \$164,550 for single return filers or \$200,300 for joint returns in 2008; maximum marginal rate of 28 percent) but restore the 36- and 39.6- percent rates on the upper brackets.</p>
5. AMT	Supports extending annual patch.
6. Payroll tax	Beginning “a decade or more from now,” increase maximum amount of earnings subject to Social Security payroll tax (\$106,800 in 2009) with “donut hole” for middle-income taxpayers. Tax would resume for incomes above \$250,000 at a rate of two percent to four percent including employer and employee share.
7. Health care	Provide a new refundable 50-percent tax credit on employee health insurance premiums paid by small business employers.
8. Education	<p>Provide a fully refundable \$4,000 college tax credit available at enrollment (by using prior year’s tax data).</p> <p>Allow families to apply for financial aid by checking a box on their tax form and authorizing their tax information to be used.</p>

9. Retirement saving	<p>Eliminate income taxation of seniors earning less than \$50,000.</p> <p>Provide automatic enrollment in employer plans and automatic roll-over to new employer's plan.</p> <p>Require employers without plans to enroll employees in direct-deposit IRA accounts.</p> <p>Establish new savings plans for the self-employed and new small businesses and allow IRS to deposit tax refunds into plans.</p> <p>Expand saver's credit to match 50 percent of first \$1,000 of savings for families that earn under \$75,000, make tax credit refundable, and automatically deposit match into designated personal accounts by using account information listed on IRS tax filings.</p>
10. Housing	<p>Provide a refundable, 10-percent mortgage tax credit for non-itemizers.</p> <p>Provide \$10 billion in additional mortgage revenue bonds for foreclosure refinancing and low- and moderate-income first-time homebuyers.</p>
11. Families	<p>Provide a refundable income tax credit to offset payroll tax on first \$8,100 of earnings: up to \$500 per person and \$1,000 per family. Credit also would apply to self-employed small business owners.</p> <p>Expand the child and dependent care tax credit by making it refundable and increasing the credit from 35 percent to 50 percent of child care expenses for low-income families.</p> <p>Expand the earned income tax credit (EITC).</p>
12. Simplification	<p>Provide optional pre-completed tax forms (based on financial information IRS receives directly from employers and banks) for taxpayers to verify, sign, and return to the IRS or file on-line.</p>
IV. Other tax proposals	
1. PAYGO and expiring provisions	<p>In general, enforce congressional "pay-as-you-go" (PAYGO) budget rules, which require new spending or tax cuts to be paid for by spending cuts or tax increases.</p> <p>However, score tax proposals against "current policy" baseline that assumes expiring tax cuts will be extended; no offsets required to extend these cuts.</p>

Other Obama Administration priorities

Once economic recovery legislation is addressed, it is unclear on what issues the Obama Administration will choose to focus next. During the election campaign, President-elect Obama focused on priorities such as middle-income tax relief, healthcare reform, climate change, and energy independence.

Healthcare reform

President-elect Obama has pledged to make universal healthcare coverage one of his Administration's top priorities. The number of uninsured Americans continues to grow, as do healthcare costs, which are at 16 percent of GDP and rising.

President-elect Obama has named former Senate Majority Leader Tom Daschle (D-SD) to be Secretary of Health and Human Services. Daschle also will oversee a new White House Office of Health Reform. In both these roles, Daschle will lead President-elect Obama's efforts to enact healthcare reform legislation.

In particular, President-elect Obama has proposed implementation of a series of policies intended to provide coverage to individuals unable to purchase health insurance, while not significantly disrupting coverage for the 85 percent of Americans who have health insurance.

President-elect Obama's proposals include tax subsidies for the 15 percent of Americans who are uninsured and for small businesses that cannot afford to offer health coverage to their workers. Regarding the latter, President-elect Obama has proposed creating a new refundable 50-percent tax credit for employee health insurance premiums paid by small business employers. President-elect Obama also has proposed creation of as-yet unspecified penalties for employers that do not provide coverage and for parents who do not obtain coverage for their children.

During the election campaign, President-elect Obama criticized a proposal by Republican presidential candidate Senator John McCain (R-AZ) intended to eliminate a perceived "bias" toward employer-sponsored health insurance by replacing the exclusion for employer-provided health coverage with a \$2,500 health insurance tax credit (\$5,000 for families). However, Senate Finance

Chairman Baucus, while not calling for repeal of the exclusion, has suggested the need to consider possible reforms. Chairman Baucus has released a white paper outlining his goals for healthcare reform, including a refundable health insurance tax credit. He also has entered into discussions with the Senate Health, Education, Labor and Pensions Committee. In addition, Chairman Baucus could introduce comprehensive healthcare reform legislation early in the 111th Congress.

Energy policies

Policies of new Administration

Energy and related environmental policies are expected to be a major focus for the 111th Congress and the Obama Administration. During the election campaign, President-elect Obama proposed a goal of deriving 10 percent of U.S. electricity from renewable sources by 2012 (25 percent by 2025). He also proposed adding one million plug-in hybrid vehicles that can get 150 miles per gallon by 2015 and adopting an economy-wide cap-and-trade program to reduce greenhouse gas emissions by 80 percent by 2050.

Congress and the Administration are likely to focus on CO₂ emissions in drafting new energy policies. Under the cap-and-trade program proposed by President-elect Obama during the campaign, the government would auction allowances to emit a fixed amount of greenhouse gases. The Senate considered cap-and-trade legislation in 2008 that would have allocated 75 percent of emission allowances free of charge and auctioned the balance. That legislation would have set the level of allowances such that greenhouse gas emissions would be reduced by 19 percent below 2005 levels by 2020 and 71 percent by 2050. Similar legislation may be considered in the 111th Congress.

The Emergency Economic Stabilization Act of 2008 directed the Treasury Department to commission the National Academy of Sciences to study and report by October 2010 on the impact of the tax code on greenhouse gas emissions. This study could generate new issues and provide some impetus for consideration of reforms of tax provisions that have a significant impact on energy and the environment.

Although the first order of business for the Obama Administration likely will be an economic recovery plan, that legislation could include energy-related provisions, such as longer-term extensions and modifications of alternative energy credits, energy efficiency incentives, and federal funding of local government spending on energy conservation and energy infrastructure to stimulate employment.

Key energy policymakers

President-elect Obama has announced the appointments of several individuals who will help shape his Administration's energy policy.

Dr. Steven Chu, a Nobel Prize-winning physicist from the Lawrence Berkley National Laboratory, has been named as Energy Secretary. In addition, President-elect Obama tapped three former Clinton Administration Environmental Protection Agency (EPA) officials to other key posts. These include Carol Browner, the former EPA Administrator, to serve as energy policy advisor in the White House; Lisa Jackson, who worked at the EPA under Browner and currently heads the New Jersey Environmental Protection Department, to be the new EPA Administrator; and Nancy Sutley, who also worked for Browner at the EPA, to chair the White House Council on Environmental Quality.

In Congress, Rep. Henry Waxman (D-CA) will replace Rep. John Dingell (D-MI) as chairman of the House Energy and Commerce Committee. In the Senate, Jeff Bingaman (D-NM) is expected to continue as chairman of the Energy and Natural Resources Committee.

Climate change

With a new round of international negotiations over greenhouse gas reductions scheduled for December 2009 in Copenhagen, the Congressional session beginning this year may see renewed attention to climate change issues. President-elect Obama has supported a cap-and-trade program, as have most members of the Democratic Congressional leadership. At the state level, the Regional Greenhouse Gas Initiative now requires utilities in 10 Northeastern and mid-Atlantic states to participate in a carbon dioxide cap-and-trade program, and California is moving ahead with implementation of its Global Warming Solutions Act, which calls for a statewide cap-and-trade program by 2012.

Another alternative proposed by some to incentivize reductions in greenhouse gas emissions is a carbon tax. During the 110th Congress, Rep. John Larson (D-CT) introduced a proposal to impose a tax on carbon-based fuels such as coal, petroleum, and natural gas based on the amount of carbon dioxide emitted when such fuels are consumed. Under this proposal, the tax would start at \$15/ton of carbon dioxide emitted and increase annually by the percentage increase in the consumer price index plus 10 percent.

A federal greenhouse gas program may raise a number of policy issues that lawmakers would need to address, including the following:

- **Auctioning vs. allocation of emissions allowances.** Emissions allowances either can be allocated to existing emitters or made subject to an auction process. Because the value of these allowances is significant—an estimated \$1.2 trillion over the first 10 years of the program proposed under one Senate bill (S. 2191)—these decisions are likely to attract intense scrutiny from the business community.

- **Use of proceeds.** Either a carbon tax or an auction of emissions allowances may generate significant new federal revenues which could be used for a variety of purposes, including incentives for “green” technologies, payments to lower-income households to redress the regressivity of carbon pricing, or reductions in business or personal taxes (a so-called “green shift” in the tax base).
- **Trade and competitiveness concerns.** Imposing a carbon price on U.S. producers may disadvantage them relative to competitors in jurisdictions where carbon emissions are not restricted. S. 2191 proposed a requirement that importers purchase emissions allowances for CO₂ emissions associated with the manufacture and transport of imported goods; one issue raised was whether such a requirement would be compatible with World Trade Organization procedures. Also, since the bill would not relieve exports from the cost of emission allowances, another issue raised was the competitiveness of U.S.-made goods in foreign markets.
- **Conforming changes to other laws.** Adoption of a new system of tradable emissions allowances may require corresponding legislative or regulatory changes to both securities and tax laws.

Expired and expiring tax provisions

A number of temporary tax incentives are scheduled to expire after 2009, including the research tax credit, the subpart F exception for active financing income and “look-through” treatment of payments between related controlled foreign corporations (CFCs). In addition, certain individual tax relief provisions, including the state and local sales tax deduction and college tuition deduction, are scheduled to expire after 2009.

The Emergency Economic Stabilization Act of 2008, enacted last fall, included a comprehensive package of tax extenders. The Act provided a two-year, retroactive extension of individual and business tax incentives that had expired at the end of 2007. The legislation also provided a one-year extension of certain business and individual tax incentives that had been scheduled to expire at the end of 2008. Extended provisions included the research tax credit, 15-year depreciation of leasehold and restaurant improvements, state and local sales tax deduction, college tuition deduction, subpart F exception for active financing income, and “look-through” treatment for payments between related CFCs.

With many popular tax provisions set to expire, Congress again may consider tax extender legislation. The timing of any tax extender legislation, however, remains unclear. In the past, Congress allowed certain extender provisions to expire and renewed them on a retroactive basis.

Figure 19. Selected expiring tax provisions

Tax provision	Expires after
AMT exemption—increase over 2000 tax year amounts	2008
Nonrefundable personal tax credits permitted against AMT	2008
Additional standard deduction for real property taxes	2009
Basis adjustment to S corporation stock for property contributed to charity	2009
Biodiesel and renewable diesel fuels credit	2009
Charitable contributions of IRA distributions for individuals age 70 1/2 or older	2009
Credit for increasing research activities	2009
Election to expense environmental remediation costs	2009
Election to expense U.S films and television production costs	2009
Exception under subpart F for active financing income	2009
First-time homebuyer credit for District of Columbia	2009
Leasehold improvements and restaurant property treated as 15-year property	2009
Look-through treatment of payments between related CFC's	2009
New energy efficient home credit	2009
New markets tax credit	2009
Qualified tuition and related expenses	2009
Special rules for foreign shareholders that invest in regulated investment companies	2009
State and local general sales tax deduction	2009

Estate tax legislation

There appears to be broad consensus among policymakers that estate tax reform can and should be addressed this year, making that issue a driver of tax legislation. Under current law, the estate tax is scheduled to be repealed for decedents dying in 2010 and to be reinstated for decedents dying after 2010 at the 2002 exemption level (\$1 million) and the 2001 top rate (55 percent).

During the election campaign, President-elect Obama proposed making 2009 estate tax policy permanent, resulting in a 45-percent maximum tax rate and a \$3.5 million per-person exemption.

The estate tax has been debated in Congress in recent years without resolution. However, with the 2010 repeal looming, legislation may gain traction in 2009. Congress also may seek to address other estate and gift tax issues.

Figure 20. Estate tax rates

Year of death	Exclusion per person	Maximum rate
2001	\$675,000	55 percent
2002	\$1 million	50 percent
2003	\$1 million	49 percent
2004	\$1.5 million	48 percent
2005	\$1.5 million	47 percent
2006	\$2 million	46 percent
2007	\$2 million	45 percent
2008	\$2 million	45 percent
2009	\$3.5 million	45 percent
2010	Repeal	Repeal
2011 and after	\$1 million	55 percent

Individual AMT relief

Under the Emergency Economic Stabilization Act of 2008, individual AMT exemption amounts for the 2008 tax year were increased to \$69,950 for joint filers and \$46,200 for singles, up from \$66,250 and \$44,350, respectively, for 2007. (The Act also temporarily extended the use of certain personal tax credits, such as education credits, against the AMT.) Absent the legislation, the 2008 AMT exemption amounts would have been \$45,000 and \$33,750, respectively.

The continuation of this temporary “patch” provision for 2008, which keeps approximately 20 million taxpayers off the AMT, is estimated to reduce federal tax revenues by approximately \$62 billion. The number of AMT taxpayers will increase to more than 28 million in 2009 if the temporary AMT relief provisions are not extended again.

Airport and Airway Trust Fund

The Airport and Airway Trust Fund taxes are scheduled to expire after March 31, 2009. The aviation taxes, which fund the operations of the Federal Aviation Administration (FAA), were extended on a temporary basis because Congress was unable to pass a multi-year FAA reauthorization bill that included proposed changes to the existing aviation taxes.

The Trust Fund is credited with revenue from system users through the following dedicated excise taxes:

- 7.5-percent tax on domestic airline tickets;
- \$3.60 domestic passenger segment tax (excluding flights to or from rural airports);
- 6.25-percent tax on the price paid for transportation of domestic cargo or mail;
- 4.4 cents-per-gallon tax on domestic commercial aviation jet fuel;
- 19.4 cents-per-gallon tax on domestic noncommercial aviation gasoline;
- 21.9 cents-per-gallon tax on domestic noncommercial aviation jet fuel;

- \$16.10 per-person tax on international arrivals and departures;
- 7.5-percent tax on mileage awards (frequent flyer awards tax); and
- \$8 per-passenger tax on flights between the continental United States and Alaska or Hawaii (or between Alaska and Hawaii).

Trust Fund revenues primarily depend on the price of tickets (the domestic ticket tax) and the number of passengers (the domestic ticket tax, the domestic passenger segment tax, and the international passenger tax). The ticket tax is the largest single source of revenue, followed by the passenger segment tax and the international departure/arrival taxes.

During the 110th Congress, the House passed an FAA reauthorization bill that would have extended all the current air transportation and aviation fuel taxes through September 30, 2011. The legislation also would have increased general aviation fuel taxes. The Senate, meanwhile, failed to pass an FAA reauthorization bill. The Senate version would have increased the general aviation jet fuel tax from 21.8 to 36 cents per gallon, treated partially (fractionally) owned aircraft as general aviation for tax purposes, and eliminated the tax-exempt status of some light jet aircraft.

Other possible tax legislation

Education incentives

Congress may consider proposals to consolidate existing education incentives, expand Coverdell education savings accounts, and modify provisions relating to college savings plans. During 2008, bills were introduced in both the House and Senate that would replace the Hope and Lifetime Learning tax incentives with a single higher education opportunity tax credit. Both versions would have limited the amount of the benefits and provided for a phase-out of the credit for incomes over a certain amount. The consolidation of current incentives into one credit is intended to make it easier for students and their families to understand and use the incentive and therefore lower the cost of higher education.

During the 110th Congress, legislation also was introduced in the Senate that would have expanded Coverdell education savings accounts to include home school education expenses and increase the contribution limit for such accounts after 2008. In addition, two bills were introduced in the House that would have modified provisions relating to college savings plans. The first would have allowed nontaxable employer matching contributions to college savings plans. The second would have permitted distributions from individual retirement plans to be contributed to college savings plans without including the distribution in gross income.

Exempt organizations

Colleges and universities. Some members of Congress have proposed that colleges and universities should be required to pay out a certain percentage of their endowments each year. During 2008, Senate Finance Committee Ranking Member Grassley and Rep. Peter Welch (D-VT) held a forum on ways to maximize the use of endowment funds to make higher education more affordable. The “roundtable” meeting followed Senator Grassley’s call earlier in the year for a five-percent payout of college and university endowments and Rep. Welch’s support for a similar requirement.

Nonprofit hospitals. In recent years, some in Congress have scrutinized nonprofit hospitals and questioned whether they are providing adequate public charity medical care and community benefits to justify tax-exempt status. According to an IRS report issued in 2007, many nonprofit hospitals spend less than three percent of their annual revenue on charity medical care. In an attempt to increase that percentage, one bill introduced last year would have created a new tax credit for physicians who provide charity medical care on a volunteer or pro bono basis.

Tax administration and simplification

Government withholding. The House last year passed legislation to delay until 2012 the withholding requirement on payments to government contractors. The requirement, which was included in a 2006 law addressing the “tax gap,” is scheduled to take effect in 2011. Business groups argue that withholding is unfair to many contractors that will not owe the amount withheld and deprives them of cash flow needed in light of current economic conditions. They also argue the requirement will cost the federal government more than it would collect in taxes.

Employer-provided cell phones. Legislation passed last year by the House would remove cellular phones from the definition of “listed property,” thereby eliminating certain limitations on the tax deduction for employee use of cell telephones as well as the burdensome requirement for employees to keep detailed records of calls made on employer-provided cell phones.

Private tax debt collection. The House may revive legislation considered last year to repeal the IRS private tax debt collection program. During the 110th Congress, the House twice passed legislation to repeal a 2004 law allowing the IRS to use private-sector debt collectors to collect delinquent federal income taxes. The Senate did not consider similar legislation.

Tax treaties

Last year, the Senate approved a protocol to the U.S.-Canada income tax treaty and new U.S. tax treaties with Iceland and Bulgaria. All three tax agreements entered into force on December 15, 2008.

The United States has signed a proposed tax treaty with Malta and a protocol to the U.S.-New Zealand income tax treaty, and it is expected that a protocol to the U.S.-France income tax treaty could be signed by early 2009. It is anticipated that all these agreements will be sent to the Senate for review and ultimate ratification in 2009. Typically, the Senate Foreign Relations Committee holds a tax treaty hearing in the late spring or summer followed by Senate floor action in the fall.

An agreement with Norway for a new or revised treaty is substantially complete, but one issue has blocked completion. In addition, the United States is continuing to await action by Italy on a replacement for the existing tax treaty. The new treaty was approved by the Senate in 1999 with a reservation. Italy has the option of accepting or rejecting the treaty with the reservation.

Tax treaty negotiations are under way with Hungary. Preliminary or exploratory discussions have occurred with Poland, Colombia, Israel, Vietnam, Brazil, Chile, and Taiwan.

State tax legislation

Several state and local tax issues considered during the 110th Congress could be revived during the 111th Congress. These include legislation addressing business activity taxes, sales and use taxes, nonresident withholding, and industry-specific taxes. Some of these issues fall within the jurisdiction of House and Senate committees other than the tax-writing committees.

Business activity tax nexus. Legislation proposed in the 110th Congress would establish a bright-line physical presence standard for the imposition of state and local “business activity taxes” (including income, franchise, net worth, gross receipts, and other direct taxes on business), and also would expand the reach of

protections for solicitation of sales under Public Law 86-272. While hearings were held, the bill did not move out of committee in the House. A companion Senate bill was not considered by the Senate Finance Committee.

In the 111th Congress, continuing concerns about the legislation likely will include the potential cost of the proposed nexus change to states, as well as opposition to the fundamental principles of the proposal by states and state organizations. Key committees are chaired by either opponents of the legislation or representatives of states where the revenue departments have led state opposition to the proposal. Some multistate businesses may support the proposal, however, as state courts, tax administrators, and state legislators continue a steady push for an “economic nexus” standard that could create a multistate filing obligation based on sales volume into a state.

Streamlined sales tax. States, retailers, and other business interests continue to advocate legislation that would allow states that achieve specified simplifications to the sales and use tax laws to require tax collection by non-nexus entities such as Internet and catalog sellers. Co-sponsorship of legislation by House Judiciary Chairman John Conyers (D-MI) in the 110th Congress increases the potential for movement of the proposal in 2009. Proponents argue that the legislation represents an opportunity for Congress to provide aid to the states without reducing federal revenue, as the states would be allowed to collect their own levies on remote sales.

Nonresident withholding. Businesses and states have agreed that the current patchwork of withholding obligations for employers, as well as issues in nonresident income tax compliance for employees, need to be addressed, and that federal legislation represents the best option for effectively remedying the problem. During the 110th Congress, legislation that would establish a 60-day threshold for employer withholding and nonresident income tax liability was introduced in the House and was the subject of a House subcommittee hearing. The revenue impact of the legislation has been estimated as minimal on a multistate basis, inasmuch as resident

states currently grant a credit for taxes paid by an individual in a nonresident state. General agreement on the principles of the legislation, and substantial work to date on finding common ground, suggest a greater likelihood of passage in the 111th Congress.

Industry “nondiscrimination.” Several bills were introduced in the 110th Congress that would bar states from imposing “discriminatory” taxes against certain industries, service providers, and property. One proposal that appears to have gained traction is legislation that would place a five-year ban on “new” discriminatory state taxes on cell phone services, service providers, or property.

Technical corrections

At the end of 2007, Congress enacted legislation making technical corrections and clarifications to previously enacted tax legislation. The legislation did not include two proposed technical corrections regarding the reduced tax rate on dividends from interest charge domestic international sales corporations (IC-DISCs) and the tonnage tax on shipping income. A new technical corrections bill addressing these and other issues could be developed and considered during the 111th Congress.

Tax patents

Congress may consider legislation limiting tax patents. During 2008, Senate Finance Committee Chairman Baucus and Ranking Member Grassley introduced legislation to prohibit the Patent and Trademark Office from granting patents for “common tax strategies” and “tax planning inventions.” President-elect Obama was a co-sponsor of the bill. Meanwhile, during the 110th Congress, the House passed a patent reform bill that included a provision to prohibit tax strategy patents. Both bills would have allowed patents to be granted for tax preparation software products.

Trade Adjustment Assistance

The 111th Congress is expected to consider legislation to renew and possibly expand the Trade Adjustment Assistance (TAA) program, which expired at the end of 2007. The House passed a bill in 2007 that would have increased the health coverage tax credit percentage amount from 65 to 85 percent and sunset the credit after 2009. The bill also would have authorized Treasury to designate up to 24 manufacturing redevelopment zones eligible for redevelopment tax incentives.

In that bill, the estimated cost of TAA reauthorization and expansion would have been offset by delaying for two years the effective date of worldwide interest expense allocation rules and extending the 0.2-percent FUTA surtax by three years. However, with both these revenue raisers having been partly incorporated in other, enacted legislation, Congress would need to modify these items or choose alternative measures if it decided to offset fully a TAA renewal bill.

In the Senate, the Finance Committee did not consider TAA renewal legislation in 2008. Chairman Baucus has said that he will not consider any trade legislation, such as pending free trade agreements with Colombia or Korea, until the TAA program is extended.

Congressional budget process

Fiscal year 2009 budget legislation needs to be completed before Congress and President-elect Obama begin work on the fiscal year 2010 budget process. In September 2008, a long-term continuing resolution authorized appropriations to continue operations of the Federal government through March 6, 2009. The looming March deadline will trigger action early in the 111th Congress.

The focus will shift to the fiscal year 2010 budget as soon as the fiscal year 2009 appropriations process has been completed. Congressional hearings on the President's budget proposals typically take place in February and March, after which Congress generally adopts a budget plan ("budget resolution") that provides an overall framework for consideration of subsequent tax and spending legislation for the budget period. However, if President-elect Obama follows the same timeline as his predecessors, then Congressional hearings on the President's budget proposal may not take place until April or May.

The statutory deadline for Congress to pass a budget resolution for FY 2010 is April 15, but this date often has slipped in the past. Because a budget resolution binds only Congress, it does not require the President's approval.

Budget reconciliation process

Originally intended as a way to reduce federal budget deficits, the reconciliation process has served to facilitate consideration of legislation that otherwise would face filibusters or other procedural delays. Reconciliation bills receive expedited consideration and have special procedural protections that facilitate passage. In the Senate, reconciliation bills cannot be filibustered and require a simple majority (i.e., 51 votes) to pass.

At the same time, there are important limitations associated with budget reconciliation bills. Tax cuts enacted as part of a reconciliation bill generally must "sunset" at the end of the budget period.

PAYGO

This could be a significant year for the pay-as-you-go (PAYGO) budget rules because of the current economic environment and the election results. The PAYGO rules require any tax cuts to be offset with either tax increases or reductions in mandatory (entitlement) spending. This offset requirement can be waived in both the House and Senate, but a three-fifths majority (i.e., 60 votes) is required in the Senate. PAYGO budget rules are not expected to apply to economic recovery legislation.

Long-run budget situation

Over the longer term, the budgetary pressures on the federal government will increase. The combined impact of the retirement of the baby boom population and the rapid growth in healthcare as a share of the economy will combine to increase spending under the main federal entitlement programs: Social Security, Medicare, and Medicaid (see Figure 16 on page 18).

CBO has estimated that the combined spending on these programs will exceed 18 percent of GDP by 2050, up from eight percent in 2007. To put these figures in perspective, total government revenues have averaged 18.3 percent of GDP over the past 40 years.

Long-term fiscal outlook

Most of the increase in spending is attributable to the disproportionate growth in healthcare relative to the rest of the economy. Healthcare spending has outpaced real per-capita economic growth by 2.5 percentage points over the past several decades. President-elect Obama has proposed lowering healthcare costs by investing in health IT, taking advantage of comparative effectiveness research, and focusing on prevention. If these programs are successful, the growth in healthcare spending, and therefore Medicare and Medicaid spending, could be slowed.

President-elect Obama also proposed to address the Social Security funding shortfall in part by increasing payroll taxes on high-income workers beginning “a decade or more from now.” However, these changes alone would be insufficient to solve the long-term solvency challenges of the program.

What this means for your business

The new Administration and the new Congress are expected to work on significant economic recovery legislation before turning to other priorities such as middle-income tax relief, healthcare reform, climate change, and energy.

Efforts to promote U.S. economic growth may help to focus debate on the high U.S. corporate tax rate relative to other major global competitors, but there is a risk that a revenue-neutral approach to business tax reform could increase taxes paid by certain businesses.

The rapid and unsustainable growth in annual federal deficits and long-term fiscal challenges are expected to put pressure on Congress to consider tax increases affecting both business and individuals. Extension of expired and expiring tax provisions also will have revenue costs.

Key issues may include election campaign proposals by President-elect Obama to change international tax laws that “reward corporations that retain their earnings overseas” and to provide new tax incentives for companies that “expand or start operations in the United States.” Executive compensation may continue to be an area of continued scrutiny by Congress. Renewed focus on the “tax gap” and improving tax compliance may lead to increased administrative burdens and penalties for noncompliance.

It will be critical for the business community both to monitor and participate in the legislative process as it unfolds in 2009. Business leaders should have an active voice in shaping legislation and share their knowledge of how best to promote economic growth.

Proposed revenue-raising tax provisions

Provision	Source	10-year revenue estimate (millions)
International		
Allocate expenses and taxes on the basis of foreign income repatriation	Rangel	106,390
Exempt active foreign dividends from U.S. taxation	CBO; JCT	61,300; 54,800
Modify inventory property sales source rule	CBO; Clinton	52,500; 19,250
Tax the worldwide income of U.S. corporations as it is earned	CBO	39,100
Repeal worldwide interest allocation rules	Rangel	26,214
Limit eligibility for reduced treaty withholding rates based on residency of foreign parent	House	7,478
Treat certain U.S. controlled foreign corporations (CFCs) located in “tax haven” countries as domestic companies for U.S. tax purposes	Other	5,800
Repeal deferral of U.S. income tax on income earned by the foreign subsidiary of a U.S. company that is attributable to sales in the United States	Other	4,200
Impose stricter limits on related-party interest deductions by expatriated entities	Treasury	1,655
Apply anti-corporate inversion legislation retroactively	Senate	1,241
Modify entity classification rules to reduce opportunities for tax avoidance	JCT	1,200
Amend rules for determining corporate residency	JCT	900
Terminate special DISC rules	Rangel	881
Amend 80/20 company rules	Clinton	402
Require reporting of payments to, and restrict tax benefits for, income flowing through identified tax havens	Clinton	200
Modify foreign office material participant exception applicable to certain inventory sales	Clinton	80
Grant Treasury regulatory authority to address foreign tax credit transactions involving inappropriate separation of foreign taxes from related foreign income	Senate	16
Deny the preferential maximum 15-percent dividend tax rate for certain dividends from foreign corporations	Other	N/A
Denial of deductions and credits with respect to untimely returns of non-resident aliens and foreign corporations	JCT	N/A
Compliance with earnings stripping provision	JCT	N/A
“Tax shelters”		
Clarification of the economic substance doctrine and related penalty provisions	Senate; House	10,012; 4,081
Modifications of effective dates for the application of the American Jobs Creation Act of 2004 leasing (SILO) provision—apply loss limitation to leases with foreign entities regardless of when the lease was entered into	Senate	3,235
Denial of deduction for interest on underpayments attributable to non-economic substance transactions	Senate	43

Tax accounting and corporate		
Repeal section 199 deduction	Rangel	114,930
Repeal "last-in, first-out" method of accounting	Rangel	106,510
Increase Section 197 amortization from 15 to 20 years	Rangel	20,700
Reduce NOL carryback period to one year	Senate	20,000
Repeal "lower of cost or market" inventory valuation method	Rangel	7,150
Modify dividends received deduction	Rangel	4,600
Allow RICs a dividends paid deduction for redemptions only if the redemption represents a contraction	Clinton	3,960
Treat receipt of tracking stock as property	Clinton	1,284
Modify tax treatment of certain reorganizations in which portfolio interests in stock disappear	Clinton	680
Deny deduction for punitive damages	Senate	333
Require consistent treatment and provide basis allocation rules for transfers of intangibles in certain nonrecognition transactions	Clinton	331
Eliminate double deduction of mining exploration and development costs under the minimum tax	JCT	300
Require REMICs to be secondarily liable for the tax liability of REMIC residual interest holders	Clinton	296
Limitation of employer deduction for certain entertainment expenses	Senate	290
Modify section 1031 treatment for certain real estate	Senate	281
Clarify gain recognized on certain spin-offs	Rangel	235
Prohibit C corporations from using rule for accrual service providers	Rangel	225
Denial of deduction for certain fines, penalties, and other amounts	Senate	210
Modify application of income forecast method of depreciation	JCT	100
Require accrual of time value element on forward sale of corporate stock	Clinton	91
Deny change in method treatment of tax-free transactions	Clinton	50
Modify the treatment of employee personal use of non-commercial aircraft	Senate	44
Limit dividend treatment for payments on self-amortizing stock	Clinton	20
Passthroughs		
Treat income of partners for investment management services as ordinary income	House	25,624
Modify safe harbor for allocation of nonrecourse deductions and exclude nonrecourse liabilities from outside basis	JCT	2,200
Recognize ordinary income from certain S corporations stock options	Rangel	606
Apply section 1239 to partnership interests and tax-sharing agreements to treat certain gain between related parties as ordinary	House	135
Modify application of unrelated business income tax to S corporation shareholders	JCT	<50
Modify adjustment rules for basis of undistributed partnership property	JCT	<50
Financial services		
Tax large credit unions in the same way as other thrift institutions	CBO	21,100
Disallow deduction for interest on indebtedness allocable to tax-exempt obligations	JCT	700
Capitalization of commissions by mutual fund distributors	Clinton	598
Change the tax treatment of contingent convertible debt instruments	Senate	479

Modify and clarify certain rules relating to debt-for-debt exchanges	Clinton	341
Require ordinary treatment for options dealers and commodities dealers	Clinton	233
Provide generalized rules for all income-stripping transactions	Clinton	115
Require cash-method banks to accrue interest on short-term obligations	Clinton	102
Require current accrual of market discount by accrual method taxpayers	Clinton	81
Repeal Notice 2008-83 exempting banks from limitation on certain built-in losses following ownership change	Other	N/A
Modify the tax treatment of prepaid derivative contracts	Other	N/A
Employee benefits		
Repeal pick-up rules for employee contributions to state or local governmental retirement plans	JCT	4,800
Provide that payments in redemption of stock held by an ESOP not deductible as dividends	JCT	3,400
Extend early withdrawal tax to eligible deferred compensation plans of state and local governments	JCT	1,500
Impose limitation on prefunding of welfare benefits	Clinton	1,284
Limitation on annual amounts that may be deferred under nonqualified deferred compensation arrangements	Senate	910
Modify definition of covered employee under section 162(m) for denial of deduction for executive compensation	Senate	130
Increase section 4973 excise tax on excess IRA contributions	Clinton	101
Increase elective withholding rate for nonperiodic distributions from deferred compensation plans	Clinton	69
Subject signing bonuses to employment taxes	Clinton	56
Require disclosure of employer-provided health insurance coverage on employee's annual Form W-2	Other	N/A
Employment tax		
Provide consistent FICA treatment of salary reduction amounts	JCT	164,000
Modify determination of amounts subject to employment or self-employment tax for partners and S corporation shareholders	Rangel	9,410
Extend Medicare payroll tax to all state and local government employees	JCT	5,400
Conform calculation of FICA taxes and SECA taxes	JCT	3,900
Modify FICA tax exception for students	JCT	3,300
Apply employment taxes to sales incentive payments made by manufacturers	JCT	400
Modify the rules relating to the treatment of individuals as independent contractors or employees	Other	N/A
Energy		
Repeal the expensing of exploration and development costs for extractive industries	CBO	25,500
Impose 13-percent severance tax on Gulf leases	Senate	10,600
Deny section 199 deduction for major integrated oil companies	Senate; House	9,433; 9,992
Revalue LIFO inventories of large integrated oil companies	Senate	4,332
Accelerate fuel tax on finished gasoline to the point of removal from the refinery or entry into the U.S.	Senate	824
Repeal percentage depletion for non-fuel minerals mined on federal and formerly federal lands	Clinton	823
Modify amortization for certain geological and geophysical expenditures	Treasury	667
Repeal temporary 15-year recovery period for natural gas distribution lines	Treasury	530

Increase amortization period for geological and geophysical (G&G) costs from 2 to 5 years for independent producers	Treasury	353
Exclude denaturant from alcohol fuels credit	Senate	171
Modification of credit for producing fuel from a non-conventional source	Senate	152
Repeal certain royalty relief for the oil and gas leases	House	N/A
Modify the tax treatment of oil and gas commodities and oil and gas commodities derivatives	Other	N/A
Excise taxes		
Increase excise taxes on tobacco products	JCT	91,905
Reinstate the Superfund taxes	CBO	19,100
Extend the gas-guzzler tax to vehicles with a gross vehicle weight of 6,000 to 10,000 pounds	CBO	13,000
Modify the federal excise tax on communications services—expand the tax base to all voice and data communications	JCT	11,200
Increase airport and airway trust fund taxes	Senate	3,962
Modify the federal excise tax on communications services—modernize the excise tax on voice communications services	JCT	2,000
Tax finished gasoline at refinery gate	Senate	1,099
Tax administration		
Require information reporting on payments to corporations	Treasury	6,775
Require a certified taxpayer identification number from contractors	Treasury	199
Extend statute of limitations where state tax adjustment affects federal tax liability	Treasury	48
Repeal exemption for withholding on certain gambling winnings	Clinton	42
Double certain penalties, fines, and interest on underpayments related to certain offshore financial arrangements	Senate	11
Provide reporting for proceeds of auction sales	JCT	N/A
Individual		
Provide a new standard deduction for health insurance (\$7,500 for single coverage and \$15,000 for family coverage) and repeal (1) the exclusion for employer-paid health insurance, (2) the self-employed health insurance deduction and (3) itemized medical deductions for those not enrolled in Medicare	JCT	440,080
Repeal the deduction for interest on home equity indebtedness	JCT	22,600
Provide uniform treatment for dependent care benefits	JCT	12,400
Reduce computational complexity of refundable child tax credit	JCT	3,728
Clarify uniform definition of child	JCT	2,080
Repeal exclusion for qualified tuition reductions	JCT	1,900
Conform definition of qualified medical expenses	JCT	500
Deny refundable child credit when section 911 exclusion is elected	JCT	400
Require taxpayers to include rental income of residence in income without regard to period of rental	Clinton	177
Estate and gift tax		
Eliminate non-business valuation discounts	Clinton	7,418
Determine certain valuation discounts more accurately for federal estate and gift tax purposes	JCT	3,600
Restore phaseout of unified credit for large estates	Clinton	1,413

Eliminate the stepped-up basis in community property owned by surviving spouse	Clinton	742
Curtail the use of lapsing trust powers to inflate the gift tax annual exclusion amount—disregard all Crummey powers	JCT	700
Limit perpetual dynasty trusts	JCT	300
Eliminate gift tax valuation exception for transfers of personal residences to a trust	Clinton	299
Curtail the use of lapsing trust powers to inflate the gift tax annual exclusion amount—(1) disregard Crummey powers held by non-beneficiaries or (2) disregard Crummey powers lacking substance	JCT	200
Extend pro-rata basis allocation requirement to all part-gift, part-sale transactions	JCT	100
Provide reporting for a consistent basis between the estate tax valuation and the basis in the hands of the heir	JCT	<50
Require that qualified terminable interest property for which a marital deduction is allowed be included in the surviving spouse's estate	Clinton	18
Tax-exempt organizations and bonds		
Eliminate advance refunding of governmental bonds and 501(c)(3) bonds	JCT	10,500
Subject investment income of trade associations to tax	Clinton	1,704
Modify UBTI rules for certain investment partnerships	Rangel	1,340
Eliminate private payment test for stadium bonds	JCT	700
Amend information reporting requirements to include interest on tax-exempt bonds	JCT	500
Limit tax-exempt status of fraternal beneficiary societies that provide commercial-type insurance	JCT	500
Reduce tax-indifferent shareholder's basis in stock by nontaxed portion of extraordinary dividend	JCT	200
Reform intermediate sanctions and extend certain reforms to private foundations	JCT	200
Eliminate the special exclusion from unrelated business taxable income for gain or loss on sale or exchange of certain brownfield properties	Treasury	95
Penalty for failure to file Form 5227	Clinton	17
Insurance		
Modify rules for capitalizing policy acquisition costs of insurance companies	Clinton	8,842
Require recapture of policyholder surplus accounts	Clinton	1,844
Increase the proration percentage for property and casualty insurance companies	Clinton	1,228
Disallow deduction for interest on debt allocable to tax-exempt income of insurance companies	JCT	1,200
Modify treatment of sales of life insurance contracts	Clinton	407
Disallow a deduction for "excess" reinsurance premiums paid to foreign affiliates	Other	N/A

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