WNTS Insight

A Washington National Tax Services (WNTS) Publication

November 21, 2011

"Super Committee" unable to reach agreement - fate of expiring provisions remains uncertain

Efforts to reach an agreement on $1.2 trillion in deficit reductions fell short over the weekend and today as members of the Joint Select Committee on Deficit Reduction acknowledged that they were unable to bridge differences over tax revenues and spending reductions. As part of the debt limit increase agreement enacted in August, the 12-member panel -- divided evenly between Democrats and Republicans -- had been charged by the Budget Control Act to vote by November 23 on a deficit reduction plan.

Rep. Jeb Hensarling (R-TX) and Senator Patty Murray (D-WA), as co-chairs of the Joint Select Committee, late today issued a joint statement formally announcing that "it will not be possible to make any bipartisan agreement available to the public before the committee's deadline." In their statement, the co-chairs noted that "despite our inability to bridge the committee's significant differences, we end this process united in our belief that the nation's fiscal crisis must be addressed and that we cannot leave it for the next generation to solve."

If the "super committee" had succeeded in agreeing on recommendations, those proposals would have been guaranteed an up-or-down vote without amendment in the House and Senate by December 23. However, the Joint Select Committee was unable to agree on an acceptable mix of revenues, discretionary spending cuts, and changes to Medicare and other mandatory spending programs.

Republicans on the panel stated over the weekend that Democrats were unwilling to cut Medicare, and Democrats responded that Republicans were unwilling to increase taxes on upper-income individuals. Similar disagreements were factors in derailing deficit reduction negotiations this summer between President Barack Obama and House Speaker John Boehner (R-OH), as well as the deficit reduction talks led by Vice President Joe Biden.

Congress now faces the prospect of deficit reduction being achieved through across-the-board spending reductions evenly divided between defense and most non-defense programs. The Budget Control Act requires $1.2 trillion in spending cuts to be implemented through 2021 under a process known as "sequestration" that would begin in January 2013. Debate over how to control unsustainable growth in the federal debt is expected to remain a dominant issue in 2012 and beyond.

Uncertainty remains over expiring tax provisions

Individual tax rates set to expire at the end of 2012

The inability to agree on a compromise deficit reduction package eliminates what some Republicans on Capitol Hill reportedly had viewed as an opportunity to address the expiration of current individual tax rates at the end of 2012. According to numerous press reports, Senator Pat Toomey (R-PA), a member of the Joint Select Committee, had proposed to raise as much as $300 billion in net revenues through measures that included limits on itemized deductions while at the same time permanently reducing current income tax rates by 20 percent. Under Senator Toomey's proposal, the current temporary 35-percent top rate reportedly would be fixed at 28 percent, with other rate brackets also being reduced. It has been reported that Democrats on the Joint Select Committee rejected Senator Toomey's proposal in part because it would have made permanent lower rates for upper-income individuals.

The expiration of Bush-era individual tax rates at the end of 2012 will remain a central issue in next year's elections for control of the White House and Congress. President Obama has stated that he regrets signing the 2010 legislation that extended the 2001 and 2003 tax rates across-the-board and has promised to oppose any further extension of current rates for the top two income tax brackets. Under the President's FY 2012 budget, the top individual rate is proposed to revert to 39.6 percent. The Administration also has proposed to restore estate tax rates at the 2009 level and establish a top rate of 20 percent for capital gains and qualified dividends.

Business and individual provisions set to expire at the end of 2011

It is uncertain whether any of the proposals or counter-proposals offered by members of the Joint Select Committee proposed to extend temporary business tax provisions such as the research credit that are set to expire at the end of 2011. Congress has repeatedly extended on a retroactive basis the research credit, CFC look-through, the active finance income exception, and other temporary business provisions. However, a temporary expiration of such provisions may have a financial statement impact on affected companies.

At this time, it is unclear when Congress may take up legislation to extend some or all of the expiring business tax provisions, and whether revenue provisions would be required to offset the cost of an extenders package. Last week, every member of the House Ways and Means Committee sent a letter to Chairman Dave Camp (R-MI) and Ranking Member Sander Levin (D-MI) urging Congressional action on business and individual tax provisions scheduled to expire at the end of 2011.

Other issues remaining unresolved this year include proposals to extend payroll tax relief, unemployment benefits, individual alternative minimum tax (AMT) relief, and a scheduled 30-percent reduction in Medicare physician reimbursement rates that will take effect on January 1, 2012 absent action by Congress.

Sequestration impact to vary

The Budget Control Act provides for $1.2 trillion in automatic spending cuts over nine years beginning January 3, 2013, under a "sequestration" order to be issued by the White House Office of Management and Budget. Across-the-board spending cuts are to be evenly divided between defense and most non-defense programs. Social Security, Medicaid, and certain programs assisting low-income Americans are exempted from cuts. In addition, Medicare spending reductions under sequestration are capped at two percent and can apply only to health care providers.

Agencies expected to be affected significantly include the Internal Revenue Service, which has already seen its annual budget cut by four percent. Its share of the additional sequestration budget cuts is expected to reduce the agency's budget by another seven percent. IRS Commissioner Douglas Shulman recently wrote to Congress warning about the impact of additional sequestration spending cuts on taxpayer assistance, regulatory projects, and compliance activities.

Many members of Congress and officials at the Defense Department have expressed strong concerns about the impact of sequestration on defense programs. Several members of Congress, including Senator Jon Kyl (R-AZ), who has served on the Joint Select Committee, have promised to propose legislation next year to limit the amount of defense budget cuts that would be made under the sequestration process.

President Obama has promised to veto efforts to undo the sequestration process absent bipartisan agreement on a balanced deficit reduction plan that achieves the $1.2 trillion minimum level of savings called for under the Budget Control Act. Senate Majority Leader Harry Reid (D-NV) and some members of both parties also have stated that they too will resist efforts to set aside the effects of sequestration unless Congress can agree to an equal amount of deficit reductions. Since the across-the-board spending cuts will not begin until 2013, debate over how to reduce the deficit in a more effective manner is likely to take place throughout 2012.

For more information, please do not hesitate to contact:

Brian Meighan	*(202) 414-1790*	*brian.meighan@us.pwc.com*
Drew Lyon	*(202) 414-3865*	*andrew.b.lyon@us.pwc.com*
Larry Campbell	*(202) 414-1477*	*larry.campbell@us.pwc.com*
Andrew Prior	*(202) 414-4572*	*andrew.prior@us.pwc.com*

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