

## **Budget Control Act of 2011 signed into law; tax changes left to bipartisan committee**

After a bitter partisan battle, on August 2 Congress passed and the President signed into law S. 365, the “Budget Control Act of 2011.” The initial \$1 trillion round of deficit reduction over fiscal years 2012 through 2021 doesn't include revenue hikes, but the second, \$1.5 trillion round of deficit reduction over the same years may feature fundamental tax changes as part of the work-product of the bill's newly established Joint Select Committee on Deficit Reduction (JSC).

### **JSC's Mandate**

The JSC's goal is to reduce the deficit by an additional \$1.5 trillion over fiscal years 2012 through 2021, and in finding these savings, its duties are to “provide recommendations and legislative language that will significantly improve the short-term and long-term fiscal imbalance of the Federal Government.” The Administration's interpretation of the JSC's mandate is that everything is on the table, including tax reform.

### **Possible Tax Changes**

Here are some items that have been mentioned as possible tax proposals:

1. Businesses may have to give up costly tax breaks, such as accelerated depreciation, the domestic production activities deduction, and the election to use the last-in, first-out (LIFO) inventory accounting method.
2. Industries (such as oil and gas) may have to give up some of their tax preferences.
3. In return, corporations may wind up with a modestly lower top rate.
4. In the international arena, a territorial tax regime may be adopted, there may be a repatriation holiday to induce multinationals to bring home overseas profits, and there may be crackdowns on transfer pricing tax strategies.
5. There could be a new round of loophole closers, such as a crackdown on “carried interest.”
6. Individuals may find cutbacks in key tax breaks, such as the mortgage interest deduction, in exchange for flattened and lowered tax rates.

Other issues the JSC will have to deal with include:

1. the post-2012 expiration of the Bush-era income tax cuts (including the current rate schedules, and low tax rates for long-term capital gains);
2. And the expiration of the Bush-era rules for estate and gift taxation, and the transfer tax rules in the 2010 Tax Relief Act, effective for estates of decedents dying, gifts made, or generation-skipping transfers made after Dec. 31, 2012.

The President reiterated his call for a balanced plan that includes revenue changes as well as spending cuts.

He said that

“Since you can't close the deficit with just spending cuts, we'll need a balanced approach where everything is on the table. Yes, that means making some adjustments to protect health care programs like Medicare so they're there for future generations. It also means reforming our tax code so that the wealthiest Americans and biggest corporations pay their fair share. And it means getting rid of taxpayer subsidies to oil and gas companies, and tax loopholes that help billionaires pay a lower tax rate than teachers and nurses.... Everyone is going to have to chip in. It's only fair. That's the principle I'll be fighting for during the next phase of this process.”

### **Statutory Timelines**

The Budget Control Act of 2011 carries extremely aggressive targets that Congress and the JSC are supposed to meet. Here's a summary of what has to be done and when:

1. *No later than Aug. 16, 2011* (14 days after the enactment date), the 12 members and the co-chairs of the JSC must be appointed by the majority and minority leaders of the Senate, and the Speaker and minority leader of the House, who each must appoint three members. The Speaker and the majority leader of the Senate must each appoint one member to serve as co-chair from among the JSC members.
2. *No later than Sept. 16, 2011* (45 days after the enactment date), the JSC is to hold its first meeting.
3. *No later than Oct. 14, 2011*, House and Senate committees may transmit to the JSC their recommendations for law changes necessary to meet the goal of JSC.
4. *No later than Nov. 23, 2011*, the JSC must vote on a report containing the findings, conclusions, and recommendations of the committee, as well as the estimates provided by the Congressional Budget Office (CBO), and legislative language in support of those recommendations, which must also contain a statement of the deficit reduction achieved over fiscal years 2012 through 2021. A majority of JSC members must approve the report and accompanying legislative language, and the text of the report and accompanying legislative language must be made public promptly after the vote on adoption of those matters. Any JSC member may file additional, supplemental, or minority views within 3 calendar days if the member provides notice of this intention at the time of final vote on adoption of the report and legislative language.
5. *No later than Dec. 2, 2011*, if a majority of the JSC approves a report and legislative language, they must be transmitted to the President, Vice President, the Speaker of the House, and the majority and minority leaders of the House and Senate.
6. *No later than Dec. 23, 2011*, if the JSC approves a report and legislative language, it must be voted on by both the Senate and the House of Representatives. No amendments will be considered.

### **If the JSC Fails to Approve a Report**

If a majority of the JSC members fail to approve a report and legislative language, a sequestration process (i.e., across-the-board reductions) must be implemented, with annual cuts starting in 2013. The cuts will be split 50-50 between defense and domestic spending.

The Administration has said that if the JSC doesn't approve a report, or if Congress fails to pass the JSC's recommendation, nearly \$1 trillion of deficit reduction would be achieved anyway, by letting the Bush-era tax cuts expire at the end of 2012.

### **Tax Planning Implications**

In 2010, businesses and individuals weren't certain what tax rules would apply to them for 2011 and 2012 until December 17, when the 2010 Tax Relief Act was signed into law. That pattern of uncertainty until the very last minute is highly likely to be repeated again this year, making year-end tax planning, and tax planning for a longer horizon, a guessing game at best until at least the end of this year.

If the JSC approves recommendations that include comprehensive tax reform, they are not likely to begin to go into effect until 2013. If that's the case, Congress will still need to address the host of tax breaks set to expire at the end of this year under current law.

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