Congress Closes Summer With Eyes on Fall Agenda

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As Congress wrapped up its summer’s work, lawmakers mapped out a legislative strategy for the fall and drew attention to the tax cut passed this spring — as a wonderful victory or colossal failure, depending on who you talked to.

Just before heading home, party leaders held dueling press conferences at which members praised or rejected the accomplishments of the 107th Congress so far. As House members worked overtime moving two more bills with tax provisions in the face of an expected declining surplus (see pp. 712 and 713), GOP leaders drew media attention to what they accomplished. President Bush met with Senate Republicans early in the week to praise them for their accomplishments on the $1.35 trillion tax cut (P.L. 107-16) and give them an upbeat report on what he considered a productive first six months in office. He advised them to hold the line on spending and avoid sending him pork-filled appropriations bills.

At the same time, Democrats from both chambers stressed that while their counterparts view the tax cut as a crowning achievement, they consider it a colossal mistake that will drive the nation into deficits. “Obviously, there are very different points of view of what the level of accomplishment is,” said Sen. John F. Kerry, D-Mass., in an August 2 press conference. “My friends, we are already heading to a deficit situation.” House Democrats held a special rally the same day to repeat much of the same arguments they made during the tax cut debate last spring: tax cuts were skewed toward the wealthy, would crowd out important spending priorities, and would endanger the social security and Medicare trust funds.

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Senate Budget Committee Chair Kent Conrad, D-N.D., said the diminished surplus projections have all but forced Republicans to admit that there is no money left on the table other than the trust fund surpluses. He claimed his position had been solidified by the recent announcement from Treasury that it will have to borrow billions to fund the tax rebates. (See p. 716.) “This proves the worsening condition of the budget surplus,” Conrad said. “The budget surplus is evaporated. They have run this thing amok.”

Sen. Pete V. Domenici, R-N.M., lashed out at Democratic naysayers for complaining about the dwindling budget surplus without proposing any solutions, and he said some of their rhetoric sounds as if they want to halt the Bush tax cut or even raise taxes. “The problem with these partisan activities concerning the budget surplus is that [Democrats] don’t have a solution,” he charged.

“If they don’t intend to [raise taxes], what would they do differently with reference to the surplus coming down? Do they have some cure to fix the economy?”

While the simultaneous press pitches offered previews of what is likely to come this fall, other lawmakers signaled they expect the House Ways and Means Committee to consider tax legislation that would make the tax cut permanent and reform the alternative minimum tax.

Ceasing the Inevitable Sunset

House Republican taxwriters spent part of last week gathering momentum behind plans to make permanent all the provisions in the tax bill passed in the spring. Under that bill, the tax cuts are currently set to expire after December 31, 2010.

At a press conference held outside the Capitol, House Majority Leader Richard K. Armey, R-Texas, signaled leadership’s support for moving legislation this fall. “Just in the midst of all the celebration, planning, and appreciation the American people are expressing for the fact that we were able to cut taxes, in miracles of miracles, while the nation’s budget was in a surplus, they find themselves bewildered,” he said. “We will in fact be encouraging the committee to move the legislation and it is our intention to put this legislation that sunsets the sunset on the floor of the House.”

Taxwriters Kenny C. Hulshof, R-Mo., and Paul Ryan, R-Wis., have coordinated their efforts in support of H.R. 2316 and have signed on 56 cosponsors, including Ways and Means members Kevin Brady, R-Texas, Philip M. Crane, R-III., Jennifer Dunn, R-Wash., Phil English, R-Pa., J.D. Hayworth, R-Ariz., Sam Johnson, R-Texas, Ron Lewis, R-Ky., and Rob Portman, R-Ohio. Ryan had originally introduced separate legislation that included extension of the alternative minimum tax exemption at an additional cost of $206 billion over 10 years, according to Joint Commit-
An advocate of estate tax repeal, Dunn had recently introduced legislation (H.R. 2631) that would have made permanent only the repeal of the estate and generation-skipping transfer taxes and the reduction in the maximum gift tax rate. Her bill would also accelerate repeal, gradually reducing the maximum estate tax rate — to 45 percent in 2002, 36 percent in 2003, 27 percent in 2004, 18 percent in 2005, and 9 percent in 2006 — before eliminating it altogether after December 31, 2006. Yet last week, Dunn joined forces with Hulshof and Ryan, saying Congress needed to make every provision in the bill permanent.

Although participants in the rally predicted the taxwriting committee would begin hearings as soon as September and follow them with a markup soon after, a Ways and Means spokesman could not confirm that Chairman William M. Thomas, R-Calif., endorsed the plan. He said the committee would examine expiring provisions in the code relating to treatment of nonrefundable dividends.

**U.S. TAX SYSTEM INHOSPITABLE TO FOREIGN CORPORATIONS, FEI CLAIMS**

A report released July 31 by Financial Executives International says the United States has a tax system that is inhospitable to foreign corporations.

“We can’t talk about globalization without talking about this issue,” said House Ways and Means member Amo Houghton, R-N.Y., at a press conference in Washington. Houghton said he would address the report’s recommendations in the foreign tax reform bill he is drafting.

“Taxation of U.S. Corporations Doing Business Abroad: U.S. Rules and Competitiveness Issues” was written by Carl A. Dubert, a senior manager at PricewaterhouseCoopers LLP (PwC), and Peter R. Merrill, a principal with PwC. Its research, which was last updated in 1996, finds that since then improvements have been made to the U.S. international tax system, but more are needed.

Comparing central government income tax rates from 1986 through 1995, the report finds that corporate income tax rates worldwide have been falling for the past 10 years. For example, the top corporate income tax rate in Denmark — a traditionally high-tax jurisdiction — was 50 percent in 1986, fell to 38 percent in 1991, and fell again in 1995 to 34 percent. Contrasting those rates to the United States’ 46 percent top corporate rate in 1986 and 34 percent top rate in 1991, the report concludes that the current 35 percent top rate means the United States is bucking the downward trend in corporate income tax rates, making it a relatively less-favorable country for doing business.

The report says that although the U.S. tax system offers tax credits for foreign-derived income to prevent double taxation, “In actual operation . . . the U.S. foreign tax credit system does not completely eliminate double taxation and its complexity places substantial burdens on the taxpayer.”

The report also outlines hindrances to U.S.-owned companies investing in foreign markets. “U.S. shareholders may be taxed on the undistributed profits of a foreign corporation if an anti-deferral regime applies. The U.S. tax system contains a number of antideferral regimes, each with its own set of complex rules,” it says, and argues that complexity discourages U.S. companies from investing abroad.

The report compares the tax systems of France, Japan, Germany, and the United States and outlines the advantages and disadvantages of each relative to the American system of taxation. It says France and Japan have made the most changes to their tax systems to make them beneficial to both domestic and international business.

The FEI report notes that France has a lower corporate income tax rate, and royalties and capital gains are taxed at a rate beneficial to French businesses. The French also “integrate the taxation of corporations and shareholders, mitigating the problem of double taxation” and exempt most foreign active business income from taxation, the FEI report points out.

Japan, according to the report, has a tax system much like the United States’, but provides a dividend tax credit to prevent double taxation.

— Natalia Radziejewska
personal credits on the AMT, foreign sales corporations, and possibly markup a tax package for the minimum wage bill.

A Silver Bullet for AMT

Meanwhile, a bipartisan group of House taxwriters introduced a custom-built bill designed to lighten the tax load for technology employees facing substantial alternative minimum tax bills thanks to what one lawmaker is dubbing a “perfect storm.” House Ways and Means Committee member Richard E. Neal, D-Mass., has put together a narrowly tailored AMT bill that could save unsuspecting taxpayers (specifically those behind the reformAMT.org movement) who got caught in the AMT web because they exercised lucrative incentive stock options in 2000 only to watch their stock holdings tank during the recent stock market plunge.

The legislation, cosponsored by fellow taxwriters Jerry Weller, R-Ill., Robert T. Matsui, D-Calif., Lloyd Doggett, D-Texas, Dunn, and Earl Pomeroy, D-N.D., as well as Reps. Zoe Lofgren, D-Calif., and Thomas M. Davis, R-Va. (who earlier this year proposed H.R. 1487, a broader AMT/ISO bill that has so far stalled in Congress), would change the valuation of the tax preference on ISOs by allowing taxpayers to only pay taxes on the basis of their stock at the point of exercise (retroactive to January 1, 2000) minus the fair market value of the stock as of April 15, 2001, or on any gains realized at the point of sale. Sen. Joseph I. Lieberman, D-Conn., (who has introduced a similar bill, S. 1142, already this session) unveiled companion legislation in the Senate. This onetime AMT fix is projected to cost $1.3 billion over 10 years.

Under current law, AMT liability is calculated by taking the difference between the exercise price and the fair market value of the stock at the time of exercise.

Neal said he believes the bill has a “reasonable chance of enactment,” estimating that it could fit on any minimum wage proposal or end-of-the-year omnibus tax bill because of its pared-back price tag, but added that some offsets were being considered as well. “This is not a costly item,” he said. “Perhaps we could close a loophole to pay for it.” A Neal aide said staff were not considering using the Doggett shelter bill as an offset, but were working out alternative revenue raisers with the Joint Committee on Taxation. (For related coverage, see p. 712.)

According to lawmakers, the bill will not wipe out all the debts accrued by those workers who are suffering under the weight of their AMT bills, but will level the playing field a bit more. ReformAMT.org members had originally been pursuing a retroactive exemption of ISOs from consideration of the AMT or for the creation of a refundable AMT credit in the year of exercise, but see this new bill as a step in the right direction.

Neal, who has advocated abolishing the AMT for several years but blames the cost of full repeal for stymieing most of his efforts, said he crafted this particular bill because of the widespread nature of the problem, the severity of the penalties, and the need for immediate relief for taxpayers caught off guard by the AMT.

“This is probably the right temporary solution,” a Neal aide said, adding that the legislation would provide no benefit for taxpayers who made money on their ISO stocks, but provides progressive amounts of relief for those who lost a little to those who lost a lot. While the aide admitted that generally the Ways and Means Committee does not favor retroactive fixes, Treasury officials have told Neal that the Bush tax cut and energy bill have both established precedent for the retroactive provision in his AMT bill.

Neal has put together a narrowly tailored AMT bill that could save unsuspecting taxpayers who got caught in the AMT web because they exercised lucrative incentive stock options.

Cosponsor Rep. James P. Moran, D-Va., said the bill was needed to correct an egregious mistake in the tax code that was striking taxpayers it was obviously never intended to affect while also undercutting the workforce of the next millennium. “We’ve got to change the tax code,” he stated. “We’ve got to make it work in this new economy.”

Cosponsor Rep. Thomas M. Davis, R-Va., noted that while critics assert the taxpayers in question simply want to dodge their legitimate tax bills, the unintended consequences of the current AMT treatment of ISOs can lead to outlandish tax debts. “I think everyone can agree that paying your ‘fair share’ should not include driving people into bankruptcy or despair,” he stated.

Legislative Odds and Ends

After months of stagnation, the House cleared the way for a bicameral conference on a bankruptcy bill that contains 20 tax provisions and will make it harder for individuals to discharge their debts. Republicans named conferees as follows: Reps. F. James Sensenbrenner Jr., Wis., Henry J. Hyde, Ill., George W. Gekas, Pa., Lamar S. Smith, Texas, Steve Chabot, Ohio, Bob Barr,
After months of stagnation, the House cleared the way for the final stage of the legislative process on a bankruptcy bill that contains 20 tax provisions.

The House also approved by a vote of 384-33 a bill (H.R. 1140) that would provide favorable tax treatment to railroad employees, retirees, and their beneficiaries. The bill would eliminate the supplemental annuity tax on railroad employers and employee representatives and lower the payroll tax rate on railroad employers (the Tier II tax rate on employers would drop from 16.1 percent to 14.75 percent in 2002 and to 14.2 percent in 2003). The Congressional Budget Office estimated the federal revenue loss on the legislation to be $4 billion over 10 years.

The bill would also reduce the retirement age of railroad employees to 60, shorten the vesting requirement for workers and qualified spouses from 10 years to 5 years, and increase railroad retirement annuities payable to some widows and widowers of railroad employees.

Ways and Means member Sam Johnson, R-Texas, had complained that the bill would raid the social security and Medicare trust funds by $15 billion in its first year and an additional $7 billion over the next 10 years. Johnson also objected to the bill’s creation of a tax-exempt investment trust that would be authorized to invest the reserves of the railroad retirement system in non-Treasury securities, such as publicly traded stocks in private companies. Senate Republicans vowed to block the bill from reaching the floor.

Also pending in the Senate is President Bush’s so-called faith-based initiative. In hopes of reenergizing the issue, Lieberman and Senate Republican Conference Chair Rick Santorum, R-Pa., reintroduced the tax portion in new legislation (S. 1300) that aims to encourage foundational and corporate charitable giving. Santorum said the bill had widespread support but would have to take a back seat to energy and education bills for the time being. Still, he predicted that the faith-based tax initiatives would make it through the Senate by early next year.