The Year Ahead: Tax Reform - No; Tax Extenders - Yes

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Two events at the very end of last year set the stage for this year in terms of taxes and Washington – the appointment of the Chairman of the Finance Committee, Senator Baucus (D-MT), to be Ambassador to China and the introduction of a "clean" tax extenders bill by Senate Majority Leader Reid (D-NV). In short – tax reform isn't going to happen this year and tax extenders will (and they will be retroactive).

Tax Reform

Certainly the two Chairmen of the tax writing committees — Senator Baucus and Congressman Camp (R-MI), Chairman of the Ways and Means Committee — should be commended (as well as their hard working staff) for putting forward detailed proposals on certain areas of tax reform.

For the Finance Committee, they've recently caught up with the earlier work of the Ways and Means Committee putting forward detailed discussion drafts on reforming taxes including energy, tax administration, international tax.

The Ways and Means Committee had earlier put forward its own thoughtful proposals on international tax, pass-throughs (which I discussed in an earlier column) and financial products.

However, with Baucus now saying zai jian to Washington, it only underscores the growing reality that tax reform is not going to be happening this year.

The simple, cold truth is that the administration has little to no interest in tax reform (unless the House Republicans will agree to raise hundreds of billions of dollars in new revenue – i.e. tax increases – "Hey, I'll meet you at the teacup ride in Fantasyland"). Further, the leadership on both sides of the Capitol is nervous about tax reform – especially not being keen on asking members to take hard votes on legislation that doesn't look like it's going to become law. Adding to problems – many business leaders are not pleased with some of the early reform proposals, finding that their companies are sometimes the fellow behind the tree ("don't tax you, don't tax me, tax that fellow behind the tree" – former Finance Chairman Senator Long).

The outlook is that Chairman Camp will continue his work on reform (and Chairman Baucus may release another reform paper or two before jetting off to Beijing) through the year but with an eye towards teeing up tax reform for the next Congress – when Congressman Brady (R-TX) or possibly Congressman Ryan (R-WI) takes over the gavel of Ways and Means (assuming the Republicans keep the House).

Senator Wyden (D-OR), who takes over the Chairmanship of Finance, has long had an interest in tax reform, but no early indications that he has bought into the framework put forward by Senator Baucus.

In short – no tax reform this year and even next year depends a great deal on the mid-term elections and ultimately whether the White House is willing to come to the table and make reform a priority.

Tax Extenders

So where does that leave us with tax extenders? As a reminder tax extenders are some 60 or so provisions that expired at the end of 2013 including the highly popular Research and Development (R&D) Tax Credit (still under utilized by small and medium businesses, as I noted in an earlier column); dozens of other business tax provisions; a number of energy tax provisions (such as the 179D provision for energy efficient commercial buildings that has been a lifesaver for architects, engineers and contractors) as well as individual tax provisions (ex. the deductibility of sales and use tax – important for the states without personal income tax – like Nevada, home of Majority Leader Reid) and charitable giving (ex. charitable IRS rollover).

Tax extenders have been extended numerous times – as the Congressional Research Service noted in a recent report, the R&D tax credit has been extended 15 times since it was first enacted in 1981. Other tax provisions have similarly been extended time after time. Why? Because the tax extenders are popular with Congress, popular with businesses and individuals, but not popular are the policy issues that go with making the tax extenders permanent.

The most important signal on tax extenders was Senate Majority Leader Reid's introduction of legislation late last year that was a "clean" extenders bill – meaning that all expiring tax provisions (including the energy provisions such as 179D) would be extended for a year (and given that provisions have already been expired – it would be made retroactive so that the tax policy is seamless – without a break – which is what has been done with extenders in the past).

The action by Leader Reid indicates that tax extenders will be a priority for the Senate. While there is an outside chance the Senate may take up tax extenders sooner rather than later (as an amendment to the Medicare Doc Fix would be an interesting play – a must-pass bill that comes up this Spring – and sidenote:

doing tax extenders now would be a boon for the expiring commuter tax – important to Senator Schumer (D-NY)) the more likely scenario is that while the Senate acts first – it may well take until lameduck to get to final passage with the House. Why? Simple. Tax extenders are a hostage right now for tax reform. When I served on the Senate Finance Committee we repeatedly used tax extenders to help move forward (and encourage Senators' support) for tax legislation that needed some additional love. Similarly, in the House, tax extenders will be used as an encouragement for moving on tax reform.

Not to put too fine a point on it, but the day that the tax-writing committees announce that they are moving forward on extenders is the day that taps sound for tax reform. So the best bet is that late in the year the ghost will finally be given up on tax reform happening this year – and clearing the path for tax extenders to move forward. While there may be some grind in the House about offsets (and some also about extending renewable energy provisions) look for when the chimes of midnight are heard in lameduck that tax extenders goes to the President's desk for signature.

Pencils down. Tax reform — no. Tax extenders — yes.

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