

Ernst & Young Tax Educators' Symposium 2006

2006 Tax Legislative Update

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1

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2006 Tax Legislative Update

Remainder of the 109th Congress

Election 2006

Outlook for 110th Congress



Tax Legislation Enacted to Date in 2006

- Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA), P.L. 109-222 (signed into law on May 17, 2006).
- The Pension Protection Act of 2006, P.L. 109-280 (signed into law on August 17, 2006).

Tax Increase Prevention and Reconciliation Act (TIPRA)

- \$70 billion package (net 10-year cost, with \$21 billion in revenue offsets) based on 2005 budget reconciliation legislation. Major provisions included:
 - Extension of the 15% maximum tax rate on capital gains and dividends through 12/31/10.
 - Increase sec. 179 expensing from \$25,000 to \$100,000 and increase phaseout threshold from \$200,000 to \$400,000 through 12/31/09.
 - Extension of exception under subpart F for active financing income through 12/31/08.
 - Individual alternative minimum tax “hold harmless” provisions (increase AMT exemption amount for 2006; allow nonrefundable personal credits against AMT);
 - Temporary exception for look-through treatment of payments between related CFCs under foreign personal holding company income rules through 12/31/08.

TIPRA (Continued)

- Major Revenue Increase Provisions:
 - 5-year amortization of geological and geophysical expenses for major integrated oil and gas companies (+\$417 million over 10 years);
 - Increase age of minor children whose unearned income is taxed at the parent's maximum rate from 14 to 18 (+\$2.1 billion over 10 years);
 - Withholding on government payments to federal contractors who are delinquent in paying federal taxes (+\$7 billion over 10 years);
 - Eliminate income limitations on conversions of traditional IRAs to Roth IRAs (\$6.5 billion over 10 years)
 - Amend sec. 911 housing allowance (+2.1 billion over 10 years).

Pension Protection Act of 2006

- \$73 billion package (10-year net cost) containing hundreds of changes to pension and employee benefit plans:
 - Reform of funding rules for single and multiple-employer defined benefits plans;
 - Retirement savings incentives (made permanent a host of temporary provisions enacted in 2001, including increases in pension, 401(k) and IRA contribution limits;
 - Indexed income limits for traditional, spousal and Roth IRAs);
 - Made the Saver's Credit of up to \$2,000 permanent;
 - Increased PBGC premiums and guarantees.

Pension Protection Act (continued)

- Charitable Reform Provisions:
 - Tax-free distributions from IRAs for charitable purposes;
 - Enhanced deduction for charitable contributions of food inventory;
 - Increased charitable deduction limit (from 30% of AGI to 50% of AGI) for qualified conservation contributions;
 - Charitable reform package (e.g., increases in fines and penalties applicable to charitable organizations, repeal of charitable deduction for contributions of façade easements, appraisal reform, require disclosure of unrelated business income tax returns of charitable organizations).

What Didn't Get Done . . .

- The so-called “Trifecta” (H.R. 5970)
 - Permanent estate and gift tax relief
 - Minimum wage increase
 - Extenders
- The Trifecta passed the House on July 28, 2006, but failed to garner the 60 votes needed in the Senate to invoke cloture (i.e., shut off the Democratic filibuster). Further consideration has been postponed to the “lame duck” session.

Estate Tax and Extension of Tax Relief Act

- Estate and gift tax reform:
 - Reunification of estate, gift and generation-skipping taxes;
 - Increase exemption amount to \$5 million per person (fully phased-in by 2015 and indexed for inflation);
 - Allow surviving spouse to roll over unused exemption amounts;
 - Reduce maximum estate tax rates:
 - Estates < \$25 million would be taxed at capital gains rates;
 - Estates > \$25 million would be taxed at 30% rate (phased in by 2015)
 - Repeal modified carryover basis rules enacted in 2001 Tax Act (i.e., maintain “stepped-up basis for property acquired by decedent).

Extension of Expired Tax Provisions in H.R. 5970

- Modified research and development tax credit
- Modified work opportunity tax credit
- Deduction for State and local sales taxes
- Above-the-line deduction for higher education expenses
- Above-the-line deduction for out-of-pocket teacher classroom expenses
- Expensing of brownfields remediation expenses
- Availability of Archer MSAs
- New Markets tax credit
- Gulf Opportunity Zone bonus depreciation

Other Tax Provisions in H.R. 5970

- Deduction for qualified timber capital gains
- Refundable credit with respect to certain long-term unused AMT credits
- Manufacturing deduction for U.S. businesses with branches in Puerto Rico
- Mine safety tax incentives

109th Congress – “Lame Duck” Session

- Week of November 13 – December ?
- “Trifecta” or Extenders Package
- Technical Corrections
 - Identical bills introduced 9/29/06 in House and Senate
 - Open for comment until 10/31/06
- Federal Telecommunications Excise Tax Repeal (H.R. 1898/S. 1321)
- Remaining Appropriations Bills

ELECTION 2006

Balance of Power

	<u>GOP</u>		<u>DEM</u>
• HOUSE	230	15	202*
• SENATE	55	6	45*

- Includes 1 Independent
- 3 current House vacancies

2006 Senate Races (Republicans)

KYL (AZ)**

LUGAR (IN)

SNOWE (ME)**

LOTT (MS)**

TALENT (MO)

BURNS (MT)

DEWINE (OH)

SANTORUM (PA)**

CHAFEE (RI)

HUTCHISON (TX)

HATCH (UT)**

ALLEN (VA)

ENSIGN (NV)

THOMAS (WY)

** Denotes Senate Finance Committee Members

2006 Senate Races (Democrats)

FEINSTEIN (CA)

LIEBERMAN (CT)

CARPER (DE)

NELSON (FL)

AKAKA (HI)

KENNEDY (MA)

STABENOW (MI)

NELSON (NE)

MENENDEZ (NJ)

CLINTON (NY)

CONRAD (ND)**

BYRD (WV)

KOHL (WI)

BINGAMAN (NM)

CANTWELL (WA)

Tax Committee Vacancies

House Ways and Means

(24R:17D)

THOMAS (R-CA)

BEAUPREZ (R-CO)

NUSSLE (R-IA)

CARDIN (D-MD)

FOLEY (R-FL)

Senate Finance

(11R:8D:1I)

FRIST (R-TN)

JEFFORDS (I-VT)

Challenges Facing the 110th Congress

- *Budget Challenges*
- *Policy Challenges*

Budget Challenges for the 110th Congress

- Growing debt service costs
- Increase in AMT taxpayers
 - In 2005, 4 million taxpayers subject to AMT; AMT receipts totaled \$14 billion
 - By 2016, 33 million taxpayers are project to be subject to AMT; AMT receipts are projected to be \$81 billion
- Demographic Challenges
 - 26% of all U.S. residents are “Baby Boomers”
 - 2006 – the first wave of the 75 million Boomers turn 60
 - 2008 – this first wave begins to retire

Budget Challenges (continued)

- The 2001 individual income tax rate reductions are scheduled to expire in 2010
 - Maximum individual rate goes back to 39.6%
 - Dividends taxed at ordinary income rates; capital gains at 20%
 - Estate tax reverts back to maximum rate of 55%
 - Gradual repeal of PEP* and Pease** began in 2006
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- * Phase out of personal exemptions above certain income levels
 - ** Phase out of itemized deductions above certain income levels

Policy Challenges Facing 110th Congress

- Tax Reform – incremental v. fundamental, deferral v. territoriality, add-on VAT?
- “Revenue Neutral” tax bills
 - Viability of corporate revenue raisers that have been around for several years (e.g., codification of “economic substance” doctrine)
- Entitlements/Social Security Reform
- AMT repeal/reform

Questions?



Thank you for your participation and
feedback!

