



Dbriefs U presents:

The Tax Legislative Process in an Era of Debt, Deficits, and Divided Government

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Agenda

The tax legislative process

The politics of divided government

The challenge of debt, deficits, and demographics

Tax policy in the budget process

The gathering storm: Fundamental tax reform

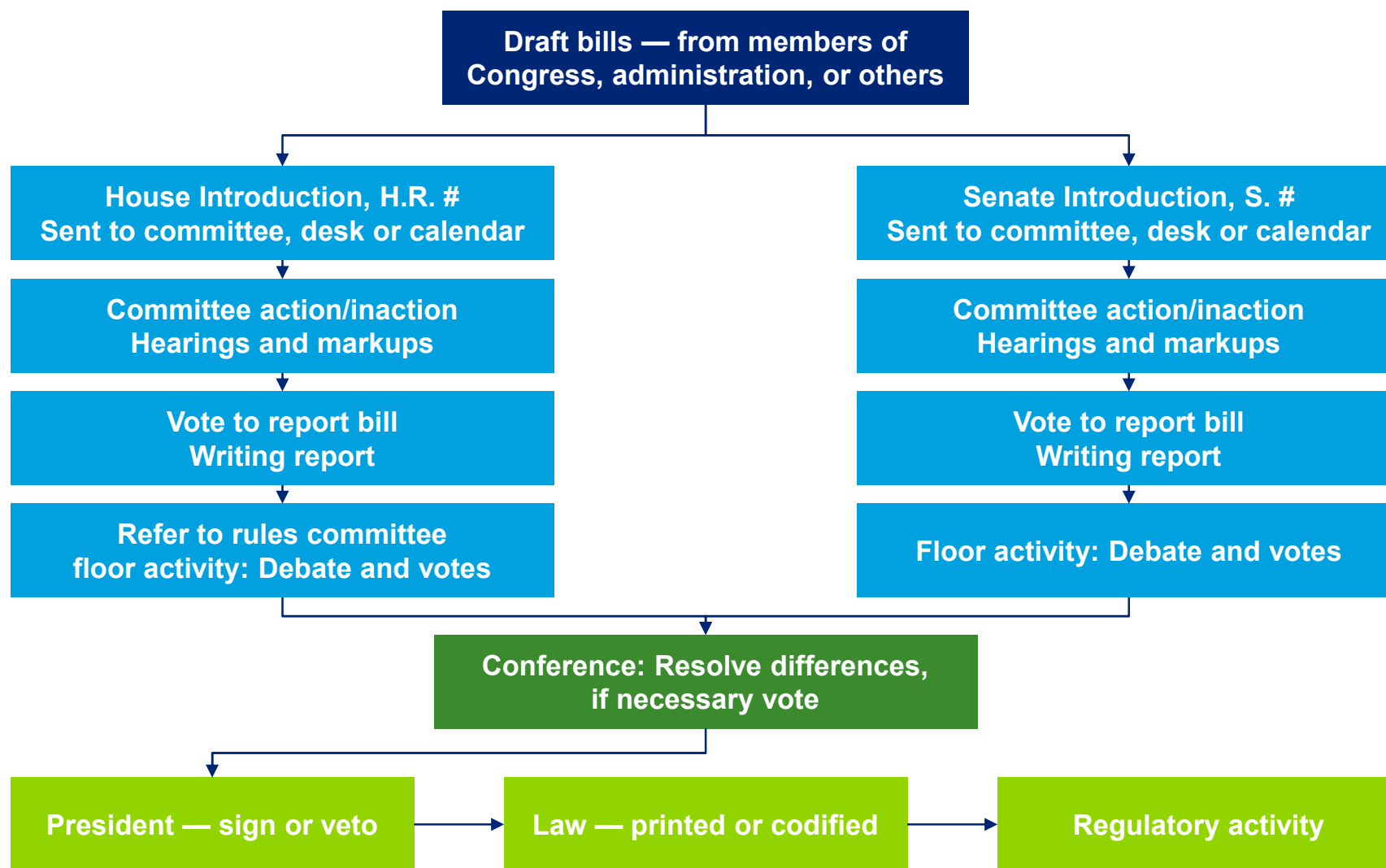
Anticipating the impact of tax reform on the tax profession

The tax legislative process

“The less people know about how sausages and laws are made, the better they will sleep at night.”

Otto Von Bismarck (attributed)

The tax legislative process — in theory



Poll question #1

Does tax legislation always originate in the House of Representatives?

- Yes
- No
- Both yes and no

Not just an invitation to struggle...

In addition to institutional design, there are a number of other factors that constrain the current tax legislative process:

- Divided government and electoral politics
- Too many “cooks” in the tax policy kitchen
- Demographic pressures and retirement of the Baby Boom generation
- Politics of debt and deficits
- Rising call for fundamental tax reform

The politics of divided government

“There is a lot of evidence... that the American people... have believed for decades now that divided government may work better than unified government.”

President William J. Clinton (Nov. 9, 1994)

Politics of divided government

- 112th Congress ushers in new balance of power in
- Washington
 - Republican controlled House
 - Filibuster creates de facto Republican control of Senate
 - WH may look for alternative routes to pursuing policy preferences
 - Regulation
 - Examination
- But does divided government = gridlock?
 - Fundamental tension of the legislative process
 - Significant non-crisis legislation is enacted through either
 - Incremental bipartisan progressOR
 - Sweeping partisan change (usually w vehicle of reconciliation)

Decentralized tax policymaking process

Are there too many cooks in the tax policy kitchen?

- **Congressional committees**
 - Ways and Means
 - Senate Finance
 - Joint Committee on Taxation
- **Congressional agencies**
 - Congressional Budget Office
 - Government Accountability Office
 - Congressional Research Service
- **Executive Branch**
 - White House
 - Internal Revenue Service
 - Treasury Office of Tax Policy
 - Office of Management and Budget
 - National Economic Council
 - WH Council of Economic Advisers

The challenge of debt, deficits, and demographics

“Blessed are the young for they shall
inherit the national debt.”

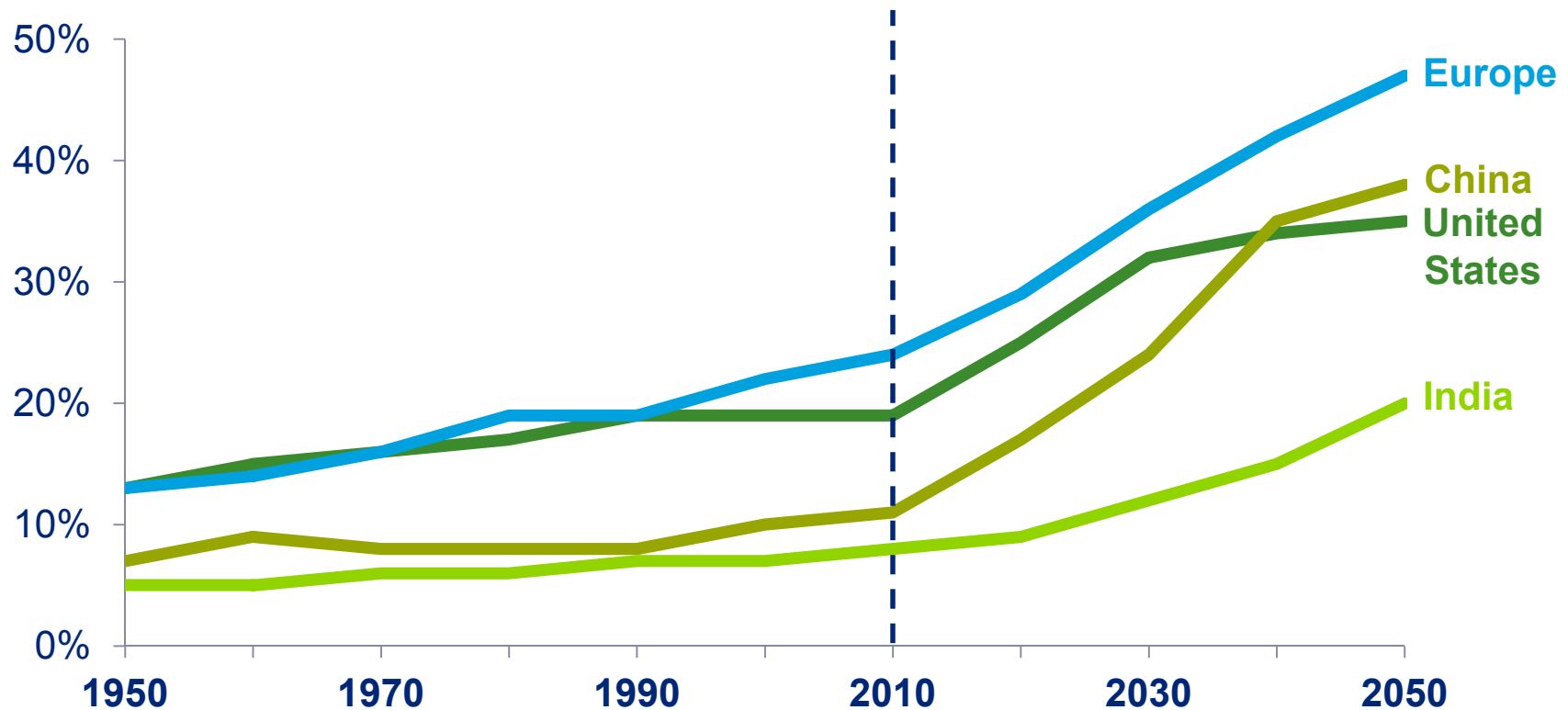
Herbert Hoover

The aging U.S. population

- Over the next 19 years, 76 million Baby Boomers will enter retirement
- Between 2010 and 2050, U.S. life expectancy at birth is projected to rise 4 years
 - Over the same period, birth rates are projected to fall by 11 percent

The retiring baby boom generation

Old age dependency ratios — historical and projected
(population 65+ / population 15–64)

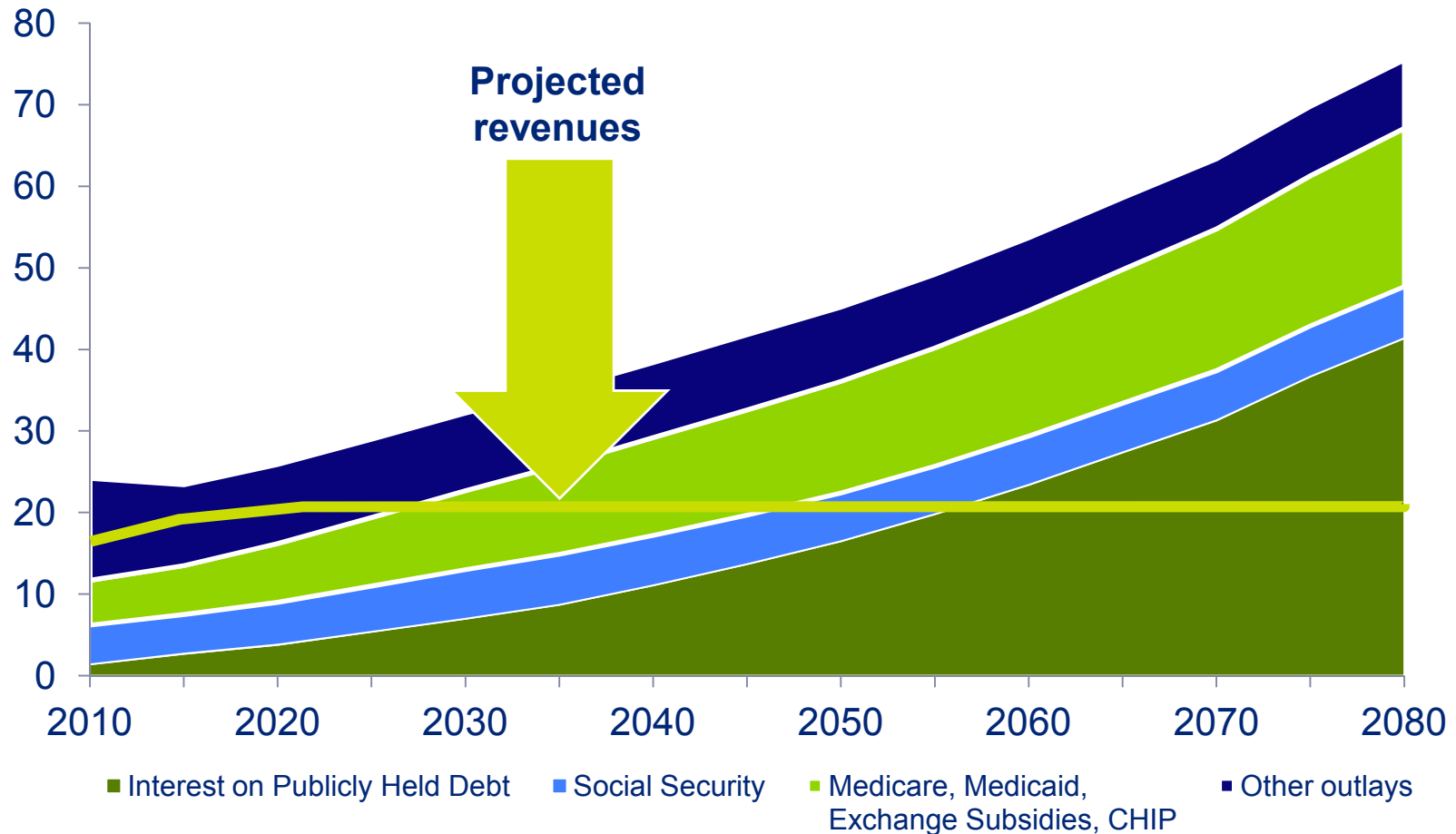


Source: United Nations, *World Population Prospects: The 2008 Revision*

The spending dilemma

- Between 2011 and 2021, spending on Social Security, Medicare, and Medicaid is projected to rise 83 percent
 - Social Security projected to go insolvent in 2036
 - Medicare projected to go insolvent in 2024
- Over the same period, interest payments on the national debt are projected to rise 250 percent
- Spending on Social Security, Medicare, Medicaid and interest on the debt are projected to swallow every dollar of tax revenue by 2025 if tax and spending policies are not changed

Composition of projected government spending (as a percentage of GDP)



Source: CBO, *The Long-Term Budget Outlook* (June, 2010), Alternative Fiscal Scenario

Poll question #2

What law established the budget process in use by Congress today?

- The Budget and Accounting Act of 1921
- The Congressional Budget and Impoundment Control Act of 1974
- The Tax Reform Act of 1986
- The Budget Enforcement Act of 1990

Tax policy in the budget process

“I’m not worried about the national debt. It is big enough to take care of itself.”

Ronald Reagan

The congressional budget resolution

- Sets revenue and spending levels for the government
- Constrains budget impact of tax and spending legislation through “points of order”
 - In Senate requires a 3/5 vote to waive
- CBO/JCT scores are vitally important
- Example: Budget resolution sets a \$2.6 trillion floor on total revenues for FY2012. Sen. Fatbottom introduces a tax cut bill that JCT says will have the effect of reducing FY2012 revenues to \$2.5 trillion. Let’s discuss the possibilities...

Budget reconciliation

- Reconciliation instructions can be included in a budget resolution passed by Congress
- Legislation moved under reconciliation cannot be filibustered in the Senate
- Directs a committee(s) to report legislation that changes law in their jurisdiction to achieve a desired budgetary outcome
- Cannot increase the deficit in years outside those covered by the accompanying budget resolution (“Byrd Rule”)
 - Means that tax cuts enacted under reconciliation often expire, thus making it difficult to predict the future path of those provisions

Pay-as-you-go and cut-as-you-go

Pay-as-you-go (“PAYGO”) law

- New mandatory spending or tax cuts must be offset (or “paid for”) by reductions in other mandatory spending or tax increases
- Exempts any legislation Congress deems an “emergency”

Cut-as-you-go (“CUTGO”) house rule

- New mandatory spending must be offset only by reductions in other mandatory spending
 - Unlike PAYGO, cannot use tax increases to pay for new spending priorities
- New tax cuts need not be offset

The gathering storm: Fundamental tax reform

“Don’t tax you, don’t tax me; tax the
fellow behind the tree”

Russell B. Long

Reforming the current tax system

- Individuals
 - Rates?
 - Improve taxpayer compliance (individuals)
 - Reduce complexity (for some)
 - Eliminate significant tax expenditures (broaden the base)
 - Eliminate special treatment for capital gains and dividends
 - An additional consumption tax (VAT, gas, carbon, sweetened and alcoholic beverages)?
- Corporate
 - Broad consensus for lowering the rate
 - Pressure to “pay for” reduced rates
 - Eliminate significant tax expenditures
 - Worldwide vs. Territorial

Raises several fundamental questions for policymakers...

Tax reform and deficit reduction together?

- Revenue neutral similar to 1986?
 - Distribution of tax burdens for individuals largely unchanged

OR

- Raise additional revenue to reduce the deficit?
 - Consequences for tax decisions

Corporate and individual tax reform together?

- Consensus begins and end with sense that corporate rate should come down
- WH wants stand alone corporate tax reform, but Congress looking to broaden to include individuals
- Factors that make corporate-only approach difficult
 - Significant business activity is taxed at individual level through pass-through entities and sole proprietorships
 - Tax benefits enjoyed by both corporate and individuals could be affected
 - Corporate-only leaves uncertainty for individual tax

What approach should govern reform?

- Reform that lowers rates and broadens the base
 - Generally maintains same level of revenue collection as share of GDP
 - Generally maintains existing distribution of tax burden across income categories
- Fundamental areas of disagreement
 - How much tax should be collected
 - Who should bear what share of the burden

Anticipating the impact of tax reform on the tax profession

“I was seldom able to see an opportunity until it ceased to be one.”

Mark Twain

Tax reform and the profession

Three distinct time periods

- **Current environment**

- Uncertainty has heightened importance of tax in many sectors
- When change comes it generally favors the young/new practitioners
 - In on the ground floor of new specialties
 - Heightened upward mobility-reform will likely accelerate retirements

- **Transition phase**

- High volume of work while clients navigate old and new systems simultaneously

- **Post-reform**

- Complexity is here to stay
- Efforts to simplify the tax code cannot also simplify the economy
- As we saw in '86 tax code will continue to be complex or get quickly re-complicated by the taxwriting committees
- No need to fear that significant changes will shrink tax practice

Poll question #3

Prior to President Obama, who was the last sitting Senator to be elected President of the United States?

- Howard Taft
- Woodrow Wilson
- Lyndon B. Johnson
- John F. Kennedy
- Teddy Roosevelt

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