Lead Tax Report

Tax Cuts

Democrats, Advocacy Groups Wring Hands Over Estate Tax, Payroll Tax Provisions

The White House continued Dec. 10 to express confidence that its tax plan will win congressional support, even as Democrats in the House and Senate continued to rail against what they called unnecessary and expensive tax cuts for the top 2 percent of all earners.

The $860 billion package debated on the Senate floor would extend through 2012 all of the reduced tax rates enacted in 2001 and 2003, extend unemployment insurance benefits for the long-term unemployed for an additional 13 months, cut workers' share of the Social Security payroll tax from 6.2 percent of earnings to 4.2 percent for one year, extend the improvements to the earned income tax credit and the child tax credit, and provide for an estate tax policy more generous than Democrats generally support.

The Senate will hold a procedural vote Dec. 13 to limit debate on a substitute amendment (S. 4753) introduced Dec. 9 by Senate Majority Leader Harry Reid (D-Nev.) and Minority Leader Mitch McConnell (R-Ky.) to a House-passed bill (H.R. 4853) to extend the Bush-era tax cuts only for individuals earning up to $200,000 ($250,000 for couples) (236 DTR GG-2, 12/10/10).

Congressional Budget Office also released its official score of the cost of the package Dec. 10, putting it at $857.8 billion over 10 years. While most of the cost is due to the tax cut provisions in the package, the extension of long-term jobless benefits was estimated to cost $56.1 billion through the remainder of fiscal 2011 and all of fiscal 2012. The initial cost of the package in its first three years, $916.9 billion, is higher than the overall 10-year costs as some tax provisions generate revenues in later years.

Although some Senate Democrats—led by Sen. Bernie Sanders (I-Vt.), who caucuses with the Democrats—spoke for hours Dec. 10 in opposition to the Reid-McConnell plan, Senate support for the package is not really in doubt, particularly after some energy- and ethanol-related provisions were added.

''You can call what I am doing today whatever you want, you can call it a filibuster, you can call it a very long speech,'' Sanders said on the Senate floor. ''I'm not here to set any great records or to make a spectacle. I am simply here today to take as long as I can to explain to the American people the fact that we have got to do a lot better than this agreement provides.''

A Senate Democratic leadership aide said once cloture is invoked, Democrats hope to reach an agreement with Republicans on how many amendments will be debated, but it is not expected to be more than a handful on both sides.

White House Still Confident. Meanwhile, White House officials reiterated their arguments that the compromise the president reached with Republicans was still the best deal that Democrats could hope to get this year.

White House Press Secretary Robert Gibbs said that the one-year extension of energy production tax credits that was added late Dec. 9 should make it an even sweeter deal for Democrats. But other, more significant changes to the compromise were off the table, he said.

The president is confident that the framework he announced is what will be voted on, Gibbs said. ''If there are changes that can be made that everybody signs onto, that's great. But I think we have, certainly for the Senate vote, a framework of what's going to move forward,'' he said.

Gibbs also argued that Democrats won more out of the compromise than Republicans. Putting aside items of mutual interest, including the business expensing provisions and extending rates for the middle-class, the president was able to secure unemployment insurance, a payroll tax holiday, a child tax credit, earned income tax credit, tax credits for college, and now energy production credits, he said.

This list demonstrates two things, Gibbs said. ''That we got, on a monetary basis, more, and that the values that we protect were ones that were tremendously important to us,'' he said.

Jason Furman, deputy director of the administration's National Economic Council, released a chart showing that—above and beyond the middle-class tax cuts—the president had succeed in getting $238 billion in ''Democratic priorities for working families and jobs,'' compared to just $114 billion in Republican priorities for high-income households.

The largest part of the deal is the payroll tax holiday for more than 155 million workers, which would provide $112 billion in tax relief in 2011, Furman stated. This compares to the second largest part of the deal, which is the extension of rate cuts for high-income families, which would provide $91 billion in relief next year, he said.

Attempts to Modify Estate Tax. Plenty of lawmakers from both parties have said the compromise includes provisions they do not like, but said the necessity of preventing taxes from increasing on Jan. 1 far outweighs their individual likes and dislikes.

For example, Senate Finance Committee member Orrin Hatch (R-Utah) told BNA Dec. 10 that he would prefer the tax cuts be permanent and the estate tax be eliminated but said ''I think most people are going to be very happy with this bill.''

The legislation includes a two-year estate tax provision that would see the tax rate—compared to the 2009 level—reduced to 35 percent and the exemption level increased to $5 million per person. The estate tax rate otherwise would return Jan. 1 to its pre-2001 level of 55 percent and the exemption level would fall to $1 million per person. According to the Joint Committee on Taxation, the two-year plan would cost $68.1 billion over 10 years.

Rep. Robert Scott (D-Va.), speaking on behalf of the Congressional Black Caucus, called the estate tax provision ''particularly offensive'' during a Dec. 10 press conference and said the CBC was working on an alternative to Obama's compromise.

The alternative includes the unemployment language as well as an additional benefit for taxpayers who have been out of work for more than 99 weeks; a payroll tax holiday or equivalent payment, such as a tax rebate check, with a guarantee that the Social Security Trust Fund would remain ''whole;'' and a two-year extension of the middle-income tax Bush-era tax cuts. Scott said the CBC plan would cost only half of the amount of Obama's plan.

CBC members expressed concern about the cost of the package and said that lawmakers serious about the deficit are eventually going to need address it and worried that what they called safety-net programs generally used by minority constituencies would be slashed down the road to pay for tax cuts for the wealthy.

''How are we going to pay for it . . . there has been no discussion,'' Scott said. ''I think you can pretty well guarantee that we're going to extend all these tax cuts . . . at some point we're going to end up paying for these and our concern is the people paying for them are the people that can least afford it.''

Rep. Barbara Lee (D-Calif.), CBC chairwoman, said the group would follow the Senate's action and determine its strategy as the debate evolves. ''Certainly there are a variety of legislative strategies and options that we're considering but at this point we don't know exactly how this will play out.''

Estate Tax Portability. Beth Shapiro Kaufman, a former Treasury Department official who has been an estate planning attorney with Caplin & Drysdale since 2001, said that while the estate tax language is an improvement over the current situation, she noted that it sets up the law to revert in 2013 to the 2001 levels of a $1 million exemption and a top rate of 55 percent.

Notably, for the first-time ever, the legislation includes language permitting estate tax portability, a measure long supported by estate tax planners that would allow a spouse to transfer his or her exemption to the surviving spouse.

Although groups such the American Bar Association have long advocated for estate tax portability, Kaufman said the provision as drafted is largely ineffective.

''It is utterly useless because in order for it to apply, both spouses have to die in the two-period it's in effect,'' she told BNA, noting that lawyers cannot draft a will based on the language. ''It's a lovely provision that promotes efficiency but it's completely useless because of its sunset.''

Shirley Kovar, a partner with Henderson, Caverly, Pum & Charney LLP, in Rancho Santa Fe, Calif., agreed that under the legislation portability would be impacted by the fact that both spouses would have to die during the window of opportunity to use the transferred exemption against the estate tax.

But Kovar, who testified before the Senate Finance Committee in 2008 and has written articles on portability, noted that portability also applies to gifts. ''I would think gift giving by surviving spouses might increase during the window when the surviving spouse can make use of the deceased spouse's exemption,'' she wrote in an e-mail exchange.

Kaufman and Kovar both said portability would need to be made permanent for it to be useful.

Payroll Tax ''Holiday'' Criticized. During his multi-hour review of the legislation, Sanders criticized the $120 billion provision that would reduce workers' share of the Social Security payroll tax from 6.2 percent of earnings to 4.2 percent in 2011 on all wages earned up to $106,800.

The amendment includes language that would transfer the equivalent amount from the general fund to the Social Security Trust Fund, but it has come under fire from some Democrats, unions, and Social Security advocates worried about the potential undermining of the program's financing.

''Social Security in my view has been the most successful federal program, in perhaps the history of our country,'' Sanders said during his filibuster on the Senate floor. ''If you divert $120 billion from the Social Security Trust Fund and you give it to workers today, what you're doing is cutting back the long-term viability of Social Security.''

During a Dec. 6 conference call with reporters, an administration official said among tax relief options, the payroll tax cuts is ''one of the higher impact tax cuts for encouraging job growth and economic growth.''

Barbara Kennelly, president and chief executive officer of the National Committee to Preserve Social Security and Medicare, criticized the provision during a briefing with reporters Dec. 10.

''As we've seen in Washington these days, it's easy to enact tax cuts but virtually impossible to allow them to expire,'' Kennelly said. ''This payroll tax holiday proposal will be no different. Election year politics in 2012 will doom this repeal of this $120 billion cut and Social Security beneficiaries will then pay the price.''

The National Treasury Employee Union found an entirely different reason for opposing the provision. In a letter sent Dec. 9 to lawmakers, NTEU National President Colleen Kelley said the tax cut would have an ''unfair and unequal impact'' on federal workers who will ''endure'' a two-year pay freeze and who also are not subject to the Federal Employee Retirement System but instead pay into the Civil Service Retirement System.

Rather than pay into Social Security, those employees pay 7 percent of their salary toward their CSRS pension. As drafted, Kelley wrote ''federal employees under that system will be seeing not only a pay freeze but the lack of a 2 percent tax cut that both private sector and federal employees covered by FERS, will benefit from''

By Heather M. Rothman and Cheryl Bolen

Texts of a summary of S. Amdt. 4753, JCT estimates (JCX-54-10) and a technical explanation (JCX-55-10), and the NTEU letter are in TaxCore. The CBO score is available at http://www.cbo.gov/ftpdocs/120xx/doc12020/sa4753.pdf

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