Trust earned.
FreedMaxick™

Obama Emphasizes Individuals, Targets Business Tax Incentives in FY 2015 Budget

President Obama renewed his call for expanding child, family and education tax credits in his fiscal Year (FY) 2015 budget proposals as well as for curbing some tax preferences for higher income individuals and businesses. The President unveiled his $3.9 trillion FY 2015 budget proposals on March 4. Many of the proposals are familiar from past budgets, but for FY 2015 the White House is placing special emphasis on passing tax reform for families and lower income individuals.

Funding for the proposed tax breaks would come from, among other sources, taxing carried interest as ordinary income, extending payroll taxes to cover certain distributions from professional service companies, and restricting the availability of like-kind exchange treatment for real estate transactions. President Obama also indicated support for reducing the corporate tax rate but, in exchange, businesses would surrender some tax preferences. In tax administration, the President proposed to stagger some return deadlines, revise the IRS's "math error" authority, and more.

IMPACT. The President's FY 2015 budget reflects the framework set out in his 2014 State of the Union Address to promote job creation and economic growth, as well as incentives targeted to lower and middle income individuals. Business tax reform, although acknowledged by administration officials as important, is not in the forefront of the President's short-term proposals. However, some targeted business proposals could gain traction, including a permanent research tax credit and extension of certain expired business tax extenders, particularly enhanced small business expensing and the Work Opportunity Tax Credit (WOTC).

COMMENT. After December 31, 2013, many tax extenders expired, including the higher education tuition deduction, the state and local sales tax deduction, the research tax credit, the WOTC, and others. House Ways and Means Committee Chairman Dave Camp, R-Mich. proposed to permanently repeal many of these popular extenders. President Obama has indicated that some of these extenders, particularly business tax extenders, could be allowed to expire in exchange for a reduction in the corporate tax rate and funding for infrastructure. One day after the President's announcement, Sen. Ron Wyden, D-Ore., the new chair of the Senate Finance Committee, indicated that the committee will take up the tax extenders in April. At a news conference following release of the FY 2015 budget, Treasury officials indicated that the fate of these extenders should be part of a discussion in Congress on broader tax reform.

IMPACT. Rep. Camp recently had unveiled his long-awaited comprehensive tax reform package on February 26 to mixed reaction. Both President Obama's proposals and Camp's plan have received a lukewarm response from the GOP, particularly in the GOP-controlled House.

©2013 CCH Incorporated. All Rights Reserved. Wolters Kluwer CCH

Tax Proposals

Although there are over 160 tax proposals within the President's FY 2015 Budget, only about 30 are new or modified from last year's 2014 Budget proposals. The viability of the many "repeat" items, however, should not be discounted in favor of what's new. Nevertheless, the Briefing gives additional focus to the new-and-revised to give practitioners a special heads up for planning purposes.

Individuals

President Obama's FY 2015 budget includes numerous changes to the tax law as it impacts individuals and families.

New/Amended Proposals

Child Tax Credit. Under the American Taxpayer Relief Act of 2012 (ATRA), the child tax credit may be refundable to the extent 15 percent of the taxpayer's earned income is in excess of $3,000. After 2017, the earned income threshold is scheduled to increase to $10,000 (indexed for inflation). President Obama proposed to make permanent the $3,000 threshold after 2017.

Child and Dependent Care Credit. The child and dependent care credit would be enhanced by providing qualified taxpayers with an additional credit on total expenses of up to $4,000 for each child under age five, capped at the total for two children. The credit rate for the additional child would be 30 percent and subject to phase-down.

IMPACT. Taken together, the current credit and the additional credit would provide a total credit of up to 65 percent of the first $3,000 in child care expenses for one child under age five and up to 65 percent of the first $6,000 in child care expenses for two children under age five.

COMMENT. The additional credit would also provide a credit of up to 30 percent on the next $1,000 in child care expenses for each child under age five, capped at two children.

Earned Income Tax Credit. President Obama proposed to increase the EITC for taxpayers without qualifying children by increasing the phase-in rate and the phase-out rate to 15.3 percent and increasing the beginning of the phase-out range. Eligible workers without qualifying children between ages 21 and 67 would be able to claim the EITC.

IMPACT. The proposal would effectively double the maximum EITC for a tax-payer without qualifying children from $500 to $1,000.

President Obama renewed his call for expanding child, family and education tax credits in his fiscal year (FY) 2015 budget proposals as well as curbing some tax preferences for higher income individuals and businesses.

ATRA previously extended a temporary increase in the EITC credit percentage for taxpayers with three or more qualifying children from 40 to 45 percent through 2017 and extended the phase-out for married couples filing joint returns by $5,000 through 2017. President Obama has proposed to make permanent both of these EITC enhancements.

IMPACT. Absent the increase in the threshold amount, a married couple filing a joint return would receive a smaller EITC than the combined amount they would receive if they were not filing a joint return.

Student Loans. Qualified taxpayers who borrow through federal programs may be eligible for student loan forgiveness under the President's proposal. Qualified taxpayers would be able to exclude from gross income amounts forgiven at the end of the student loan repayment period. A similar forgiveness provision would apply to loan forgiveness under the Indian Health Service.

Pell Grants. President Obama proposed to allow taxpayers to exclude Pell Grants from gross income, without regard to expenses they are used for, as long as the proceeds are spent under Pell Grant rules.

Conservation Easements. Current law limits the charitable deduction for conservation easements to 30 percent of adjusted gross income. A provision in effect from 2006 through 2013 raised the limit to 50 percent for most individuals and to 100 percent for farmers and ranchers. The President would make permanent the temporary enhancements that expired at the end of 2013.

IMPACT. Under current law, the 30 percent ceiling limits donors with modest incomes from deducting the full value of their conservation easement donations. Increasing the limit would increase the effectiveness of the deduction.

©2013 CCH Incorporated. All Rights Reserved.
Wolters Kluwer CCH

The FY 2015 budget also includes prior year proposals that would:

- Eliminate deductions for conservation easements on golf courses; and
- Restrict deductions and harmonize the rules for conservation easements for historic preservation.

ESOPs. The President would eliminate the deduction for dividends paid on employer stock held by an employee stock ownership plan (ESOP) that is sponsored by a publicly traded corporation.

IMPACT. The dividend deduction is most beneficial where the ESOP's ownership of employer stock is significant. However, ownership of stock in a publicly traded corporation through an ESOP is unlikely to offer significant productivity incentives to employees.

Renewed Proposals

Limitation on Itemized Deductions. As in past budgets, President Obama proposed to reduce to 28 percent the value of certain exclusions and deductions that would otherwise reduce taxable income in the 33, 35 and 39.6 percent income tax brackets. A similar exclusion would apply to taxpayers liable for the AMT.

IMPACT. The President's proposal would apply to itemized deductions after they have been reduced by the "Pease" limitation. ATRA revised the Pease limitation. The applicable threshold amounts are $300,000 for married couples filing a joint return and surviving spouses; $275,000 for heads of household; $250,000 for single individuals; and $150,000 for married couples filing separate returns. These amounts are adjusted annually for inflation.

IMPACT. The provision could find support among lawmakers who are reluctant to raise tax rates, as well as those looking to lower them within the framework of tax reform.

Buffett Rule. The President reproposed the so-called Buffett Rule. Generally, taxpayers with adjusted gross income (AGI) above $1 million would pay a minimum tax rate of 30 percent on the excess of the taxpayer's AGI over the taxpayer's modified charitable contribution deduction for the tax year.

COMMENT. Several bills to implement the Buffett Rule have been introduced in the Democratic-controlled Senate but have failed to win the necessary 60 votes for passage.

Home Mortgage Cancellation Exclusion. The temporary exclusion from income for cancellation of certain home mortgage debt expired after 2013. President Obama proposed to extend the exclusion to amounts discharged before January 1, 2017 and also to amounts discharged under an agreement entered into before January 1, 2017.

IMPACT. Many taxpayers have obtained mortgage modifications under the Treasury Department's Home Affordable Modification Program (HAMP), which has already been extended through 2015. The President's proposal would enable taxpayers who participate in HAMP through 2015 to take advantage of the exclusion. Some potential short sales this year have already been impacted by the additional tax liability to the seller for debt-forgiveness income.

AOTC. The American Opportunity Tax Credit (AOTC), an enhanced version of the HOPE education credit, is scheduled to sunset after 2017. President Obama has proposed making the AOTC permanent.

Retirement Benefits

The President's Budget proposals seek to simplify retirement-payout rules for those with modest retirement savings, as well as address several issues surrounding inherited retirement accounts. It also seeks to limit the use of tax-deferred retirement savings in certain cases involving wealthy individuals.

New/Amended Proposals

Minimum Distributions. Under the President's budget proposal, the minimum required distribution (MRD) requirements would be eliminated for individuals whose IRA and retirement plan accumulations do not exceed $100,000 in aggregate. The proposal would apply to individuals attaining age 70 ½, and individuals under age 70 ½ who die, on or after December 31, 2014. A second proposal would harmonize the application of the MRD requirements for holders of designated Roth accounts and Roth IRAs. Individuals would not be permitted to make additional contributions to Roth IRAs after age 70 ½.

IMPACT. The rules on retirement benefits aim to provide financial security for tax-payers and their spouses. The MRD rules are designed to prevent taxpayers from accumulating retirement benefits tax-free for the benefit of their heirs. Exempting taxpayers with modest balances from the MRD rules would simplify tax compliance and provide greater flexibility to draw down benefits, without compromising policy objectives. The second proposal would apply the MRD policy to Roth IRAs, to deter accumulating benefits tax-free solely for heirs.

©2013 CCH Incorporated. All Rights Reserved.

Retirement - Inherited Distributions. The President proposed to require non-spouse beneficiaries of retirement plans and IRAs to take distributions of inherited amounts over no more than five years. Certain beneficiaries, such as a disabled person or a person no more than 10 years younger than the original interest holder, can still take distributions over their life expectancy.

IMPACT. Under current law, if a retirement plan participant or IRA owner dies, the remaining benefits are payable over the life expectancy of the designated beneficiary. If there is no designated beneficiary, the interest must be paid within five years. Treasury said that retirement provisions are meant to benefit participants (and owners) and their spouses. The current rules allow non-spouse beneficiaries to accumulate earnings tax-free over long periods.

Rollovers. The President proposed to enable non-spouse beneficiaries of retirement plans and IRAs to move funds to an inherited IRA using a 60-day rollover. Current rules that require direct transfers to an inherited IRA are a trap for the unwary, serve little purpose, and generate confusion.

Renewed Proposals

Retirement Benefits Accrual. A taxpayer who has accumulated retirement benefits under various plans that exceed the amount needed for the maximum annuity permitted under current law (currently $210,000 annually) would be prohibited from further accruals and contributions.

IMPACT. Current limitations on retirement contributions and benefits do not adequately limit total accumulations through multiple plans. Accumulations can exceed amounts needed for reasonable retirement benefits that deserve tax-advantaged treatment. The system would still retain substantial tax incentives for reasonable retirement savings.

COMMENT. A similar proposal was made in the FY 2014 budget, but in an apparent nod to some complaints, the FY 2015 proposal notes that "it is anticipated that other simplifications would be considered in order to ease administration."

COMMENT. If the actuarial value of the accrued benefits decline, or if the maximum permitted benefit increases, the individual would be allowed further contributions and accruals.

Estate & Gift Taxation

In the FY 2015 budget, President Obama proposed to revisit estate and gift tax rates and other Tax Code provisions impacting estates and gifts.

IMPACT. Although ATRA made estate and gift tax rates and other changes that impact estate planning "permanent," they will remain permanent only in the sense that Congress no longer needs to vote to continue to keep them alive. However, there is no prohibition against Congress changing these provisions if the necessary votes can be mustered.

Tax Rates. As in past budgets, President Obama proposed to make permanent the estate, gift and generation-skipping transfer (GST) tax parameters as they applied in calendar year 2009. The proposal would also modify the estate tax concept of "portability."

IMPACT. The maximum unified estate and gift tax rate is set at 40 percent with an inflation-adjusted exclusion of $5 million for estates of decedents dying after December 31, 2012. The proposal would set the top tax rate at 45 percent and the exclusion amount at $3.5 million for estate taxes, $1 million for gift taxes, and $3.5 million for GST taxes. These amounts would not be indexed for inflation.

IMPACT. President Obama proposed that the revised estate, gift and GST treatment will apply after 2017. Many wills, trusts and companion instruments will need revision if these lower rates and thresholds are adopted. The current inflation-adjusted exclusion amount is $5.34 million ($10.68 million for married couples making full use of portability provisions).

Annual Gifts. The President proposed to eliminate the present interest requirement for gifts that qualify for the gift tax annual exclusion (currently, $14,000). A new category of transfers would be defined, and an annual limit of $50,000 per donor on the donor's transfers of property within this category would qualify for the annual exclusion. The new category would include certain transfers in trusts; transfers of interests in passthrough entities, such as family limited partnerships; or other transfers of property that cannot immediately be liquidated by the donee. Gifts made after the year of enactment would be subject to this treatment.

IMPACT. A donor's transfers in the new category in a single year in excess of a total amount of $50,000 would be taxable, even if the total gifts to each donee did not exceed $14,000, Treasury explained.

More proposals. Additional proposals, among others, would:

- Require a minimum 10-year term for grantor retained annuity trusts;
- Limit the duration of GST tax exemptions to 90 years;
- Coordinate certain income and transfer tax rules for grantor trusts;
- Modify the GST tax treatment of health and education exclusion trusts (HEETs);
- Expand applicability of the definition of "executor" to all tax purposes;
- Require consistency in value for transfer and income tax purposes.

©2013 CCH Incorporated. All Rights Reserved.

Small Businesses

As in past budgets, President Obama proposed tax incentives targeted to small businesses and small employers.

New / Amended Proposal

Start Up/Organizational Expenses. The deductions for start-up expenditures (under Code Sec. 195) and organizational expenditures (under Code Secs. 248 and 709) would be combined and increased. Currently, each is limited to $5,000 in the start-up year (with a reduction to the extent expenditures exceed $50,000), with a 180-month amortization of any excess. President Obama proposed to roll all expenditures into a $20,000 deduction in the start-up/organizational year, reduced to the extent expenditures exceed $120,000, then placing the excess into 180-month amortization.

IMPACT. Increasing the dollar limit on expensed new business expenditures and increasing the phase-out amount will support new business formation and job creation, according to Treasury. Consolidating the related provisions should also simplify tax administration and reduces new business owners' tax.

Renewed Proposals

Code Sec. 179 Expensing. Under the President's proposal, the Code Sec. 179 dollar limit would be permanently increased to $500,000 with a $2 million investment limit, effective for tax years beginning after December 31, 2013. Qualifying property would include off-the-shelf computer property, but not real property.

IMPACT. Under current law, the dollar limit is $25,000, with a $200,000 investment limit for tax years beginning after December 31, 2013.

COMMENT. Although extending the higher level of Code Sec. 179 expensing has been on multiple "to-do" lists reaching across party lines, legislation to make that happen has not yet materialized.

However, the expectation is that legislation, if it should pass, would be retroactive to January 1, 2014.

COMMENT. The $500,000/$2 million amounts would be indexed for inflation.

IMPACT. Bonus depreciation, at a 50-percent level, also generally expired after 2013 (subject to certain exceptions for property with longer production periods and certain aircraft). President Obama has not proposed to extend this tax break. While there is support from many members of Congress to extend bonus depreciation, its revenue impact would be considerably more significant than any extension of the Code Sec. 179 deduction, thereby reducing its probability for extension.

COMMENT. President Obama did not expressly propose extending special expensing rules for film and television production, retail and restaurant improvements, and other property. These incentives nevertheless may be part of a tax extenders bill in 2014.

Qualified Small Business Stock. The President proposed to make permanent the temporary 100 percent exclusion for qualified small business stock (QSBS), which expired for QSBS acquired after December 31, 2013. The AMT preference for this excluded gain would also be repealed.

COMMENT. The FY 2015 proposal makes two clarifications: QSBS can include stock acquired upon the exercise of warrants and options if such stock rights are acquired at original issue from the corporation; and all relevant holding periods for QSBS start on the date the stock is issued by the corporation to the taxpayer.

Code Sec. 45R Credit. The President would expand eligibility for the Code Sec. 45R small employer health insurance tax credit and simplify its operation. Instead of defining a qualified employer as an employer with no more than 25 full-time equivalent employees, the President's proposal would expand the eligible group to employers with up to 50 full-time equivalent employees. The proposal would also change the coordinated phase-outs based on average wages and number of employees.

What's New in the Administration's 2015 Budget?

President Obama's fiscal year (FY) 2015 budget contains approximately 160 proposals, 28 of which are new or significantly revised from last year's budget proposals, a Treasury official said.

HIGHLIGHTS OF THE NEW PROVISIONS INCLUDE:

- Expanding the earned income tax credit (EITC) for childless workers;
- Authorizing the Treasury and IRS to regulate paid return preparers;
- Requiring minimum distributions from some Roth IRAs;
- Consolidating the rules for deducting start-up expenses and organizational expenses;
- Capping the amount of deferred capital gain from the "like-kind" exchange of real property;
- Requiring materially participating business owners in professional service S corps, limited partnerships, general partnerships, or LLCs to pay SECA taxes;
- Preventing CFCs from shifting income from digital goods or services to low-tax jurisdictions;
- Taxing as a U.S. domestic corporation a foreign acquiring corporation with a greater-than-50-percent interest in a U.S. domestic corporation.

©2013 CCH Incorporated. All Rights Reserved.

IMPACT. The proposal aims to eliminate some perceived unfairness of the credit "to otherwise eligible small employers due to the additive nature of the credit phase-outs."

Mandatory Retirement IRA Option. Small employers without qualified retirement plans would be required to offer employees automatic enrollment in an individual retirement account (IRA). Employers with no more than 100 employees would be eligible for a non-refundable credit to defray some of the administration expenses.

IMPACT. In January, President Obama introduced the myRA retirement savings plan, directed toward lower-income individuals. MyRAs are not part of the FY 2015 Budget presented to Congress because legislation is not required to move that retirement savings plan forward.

COMMENT. Automatic enrollment at a "default" rate of three percent of an employee's compensation generally would apply to employers in business for at least two years that have more than 10 employees.

UNICAP Rules. The President would exempt employers with average annual gross receipts of $10 million or less from the uniform capitalization (UNICAP) rules for costs incurred to produce real or personal property for use by the taxpayer in its trade or business for tax years beginning after December 31, 2014.

Business-Related Revenue Raising Provisions

New Proposal

Like-Kind Exchanges. In a new proposal already having certain sectors of the real estate industry concerned, the President proposed to limit the amount of capital gain deferred under Code Sec. 1031 from a like-kind exchange of real property to $1 million per taxpayer per year. The proposal would apply for exchanges completed after December 31, 2014.

IMPACT. According to Treasury, certain properties are not eligible for like-kind treatment under Code Sec. 1031 and there is little justification for allowing special deferral treatment on the exchange of real property. Treasury objected to the development of three-party exchanges, which were not contemplated by the statute, and to exchanges of unimproved for improved real estate, which encourages "permanent deferral."

Self-Employment Tax. The President would impose self-employment (SECA) taxes on individual owners that materially participate in professional service businesses in the same manner and to the same degree, regardless of the form of ownership. Owners providing services in certain fields, including health, law, engineering, performing arts, accounting, architectural, actuarial sciences, brokerage, and consulting, would be subject to SECA taxes on their distributive shares of income. Compensation paid to owners would not be wages but would be earnings subject to SECA.

IMPACT. The taxation of employment income earned by owners of passthrough entities is outdated, unfair and inefficient, Treasury maintained. General partners and sole proprietors pay employment taxes on nearly all their earnings, while S corporation owner-employees, limited partners, and LLC members pay little or no employment tax. Taxpayers are exploiting these provisions to avoid paying Medicare payroll taxes on earnings, Treasury indicated.

Renewed Proposals

Carried Interest. President Obama again proposed to tax carried (profits) interest as ordinary income, rather than as capital gain. Much of the income is received in connection with the performance of services and is not attributable to an investment in the partnership, Treasury indicated. The partner would also have to pay self-employment taxes on the income.

IMPACT. Under current law, some service partners—including those associated with hedge funds—are paying taxes at the 20 percent rate on capital gains, rather than the rates on ordinary income. Similar proposals have failed in Congress in past years.

Punitive Damages. The President would disallow a deduction for punitive damages, whether incurred on a judgment or settlement of a claim. If insurance paid the damages, the payment would be included in gross income.

IMPACT. Treasury explained that the deductibility of punitive damages undermines their role in penalizing undesirable actions. Under current law, fines paid to the government are not deductible, and two-thirds of the amount paid for an antitrust violation may also be nondeductible.

LIFO Repeal. The FY 2015 budget would repeal the last-in, first-out (LIFO) method of accounting for inventories. For LIFO repeal, any Code Sec. 481(a) adjustment would be taken over 10 years.

COMMENT. President Obama also proposed to repeal the lower-of-cost-or-market (LCM) accounting method for inventories.

Aircraft. President Obama renewed a proposal to modify the depreciation rules for general aviation passenger aircraft, by extending the recovery period from five to seven years (12 years for taxpayers using the alternative depreciation system).

©2013 CCH Incorporated. All Rights Reserved.

Corporate and Partnership Transactions. The President also proposed to:

- Repeal the boot-within-gain limitation of current law for any reorganization having the effect of a dividend distribution;
- Conform the control test for reorganizations with the affiliation under Code Sec. 1504 to prevent taxpayers from manipulating the test to have, or to avoid, a tax-free transaction;
- Prevent the elimination of earnings and profits through distributions of certain stock;
- Expand the definition of a substantial built-in loss to prevent duplication of losses; and
- Extend partnership basis limitation rules to nondeductible expenditures.

Financial Crisis Fee. A tax-deductible fee would be imposed on U.S. bank holding companies, thrift holding companies, broker-dealers, and insured depository institutions, effective 2016. The fee would apply to "covered liabilities"— consolidated risk-weighted assets, less capital, insured deposits, and small business loans. The fee would be 17 basis points, but would be reduced 50 percent for long-term liabilities and other more stable funding items.

IMPACT. There is no specific federal tax for financial firms, although there are various fees, such as the deposit insurance fee. The law that created the Troubled Asset Relief Program requires this fee to recover costs of the financial bailout and discourage excessive risk-taking.

COMMENT. Firms with consolidated assets under $50 billion would not pay the fee.

Incentives for Manufacturing, Research & Jobs

President Obama renewed several tax proposals to encourage manufacturing, research activities and the expansion of payrolls.

Insourcing and Outsourcing. President Obama proposed a general business credit of 20 percent of eligible expenses for "insourcing" a U.S. trade or business, available to a company that reduces or eliminates a trade or business (or a line of business) conducted outside the U.S. and starts up or expands the same trade or business within the U.S. According to the administration, the proposal is designed to increase U.S. employment. The credit would be available to the U.S. parent even if the expenses were paid by a foreign subsidiary. Conversely, the proposal would disallow deductions for expenses paid for outsourcing a U.S. trade or business. Covered expenses do not include capital expenditures or costs for severance pay and assistance to displaced workers.

Research Credit. The research and experimentation credit has been a temporary "extender" provision since the 1980s. The credit expired most recently on December 31, 2013. The FY 2015 budget would make the credit permanent for expenditures after December 31, 2013, and would increase the rate of the alternative simplified credit.

IMPACT. Making the credit permanent would provide greater certainty to businesses planning or considering investment in research and development. Finding appropriate revenue offset to make this provision permanent has been a recurring issue; another extension is probable because of strong support on both sides of the aisle, while making it permanent is only likely if rolled into a larger tax reform bill.

Employment Tax Credits. President Obama proposed to permanently extend the work opportunity tax credit (WOTC) for wages paid to qualified individuals who begin work for the employer after December 31, 2013. The proposal would expand the definition of qualified veterans as a target group. The FY 2015 budget also would permanently extend the Indian employment credit for wages paid to qualified employees in tax years beginning after December 31, 2013.

IMPACT. Both credits were originally enacted in the mid-1990s, on a temporary basis, and have been extended numerous times. However, extension has been retroactive or near the expiration date, creating uncertainty for employers and potentially limiting the impact of the credit.

Targeted Growth

President Obama's FY 2015 Budget recommended enhancement or re-proposal of several tax breaks targeted to help jumpstart economic relief to specific programs or areas of the nation.

Promise Zones/Manufacturing Communities. President Obama tweaked some proposals to create economic zones and communities within which special tax breaks would be available. The centerpiece of these proposals is the creation of 20 "Promise Zones" to promote job creation and investment in economically-challenged areas. The President also called for a manufacturing communities' tax credit for communities that suffer a major loss of jobs, as well as modification of tax-exempt tribal bonds to serve similar purposes.

©2013 CCH Incorporated. All Rights Reserved.

The President proposed to limit the amount of capital gain deferred under Code Sec. 1031 from a like-kind exchange of real property to $1 million per taxpayer per year.

Regional Growth. The President also sees encouraging regional growth through enhancements of certain existing tax breaks as worthwhile proposals in his Budget. These include:

- ***Low-Income Housing Tax Credit (LI-HTC).*** The President's FY 2015 budget contains proposals relating to the LI-HTC. One proposal would allow states to convert some of their private activity bond volume cap into LIHTCs. Another proposal touted by the administration would require that owners of LIHTC-supported housing projects include protections in their agreements with state housing credit agencies for victims of domestic abuse, as required by the Violence Against Women Reauthorization Act of 2013. Other LIHTC proposals are also included.
- ***New Markets Tax Credit.*** The New Markets Tax Credit (NMTC) is a 39 percent credit for qualified investments in a community development entity. The credit expired at the end of 2013.

  The President would extend the NMTC permanently, with an allocation of $5 billion for each round. The proposal would also allow credits to offset AMT liability for investments after 2013.
- ***New York Liberty Zone.*** Legislation enacted in 2002 provided tax incentives for areas of New York damaged by the September 11 terrorist attacks. The President's proposals would provide tax credits for transportation infrastructure in or connecting to the New York Liberty Zone, from 2015 through 2024.

Investment in Infrastructure

The President urged Congress to expand the use of tax-exempt bonds as a key vehicle toward finding funds to rebuild the nation's infrastructure.

COMMENT. The cost of those proposed measures in loss of revenues, however, is not insubstantial: an estimated $6.9 billion through 2024.

America Fast Forward Bonds. The President proposed to create a new, permanent America Fast Forward Bond program. The bonds would be taxable; Treasury would pay 28 percent of the interest amount directly to the government issuer. These payments would be protected from sequestration.

IMPACT. This program follows the example of Build America Bond program, which expired at the end of 2010. Bonds with higher interest rates attract a broader market of investors.

COMMENT. Unlike last year's proposal, no special carve out for school construction is included.

Bond Refundings. As in his 2014 FY Budget, the President would provide a general tax code provision to authorize current refundings of state and local bonds, upon satisfaction of size limits and maturity limits. A current refunding issue refers to bonds used to refinance prior bonds by paying off the prior bonds within 90 days after issuing the current refunding bonds.

Private Business Use. The President would again propose an exception to the private use limits on tax-exempt bonds would be carved out for public-private research arrangements for basic research. A state or local government or private charity (educational institution) would have to own the research facilities. The owner could enter into any arm's-length contract with a private business sponsor regarding the terms of sharing economic benefits of products resulting from the research.

Governmental Ownership. The President's proposal would repeal the requirement that airports, docks, wharves and mass commuting facilities must be owned by a governmental unit, for purposes of permitting the use of tax-exempt private activity bonds.

Energy Incentives

The FY 2015 budget would extend and enhance existing incentives to encourage the production and use of "clean energy" and would renew the President's call for repeal of certain tax benefits for fossil fuels.

New/Amended Proposals

Cellulosic Biofuels. The President proposed to retroactively extend the full tax credit for cellulosic biofuels through 2020, and phase out the credit after 2024.

IMPACT. These fuels have the potential to reduce petroleum consumption and greenhouse gas emissions; extending the credit would support their availability.

©2013 CCH Incorporated. All Rights Reserved.

Energy-Efficient Homes. The FY 2015 budget would extend the current $1,000 tax credit for homes acquired prior to January 1, 2015, and would provide additional credits for constructing energy-efficient new homes through 2024.

Liquefied Natural Gas. To encourage its continued use, the FY 2015 budget would reduce excise taxes on liquefied natural gas (LNG) from 24.3 cents per gallon to 14.1 cents per gallon beginning in 2015.

IMPACT. Vehicles using LNG emit significantly lower pollution emissions, compared to diesel-powered vehicles, and help reduce petroleum consumption. Reducing the tax would promote the use of natural gas vehicles.

Renewed Proposals

Renewable Electricity Production Tax Credit (PTC). The PTC credit applies to electricity produced at qualified facilities from wind, biomass, geothermal and other sources. The President proposed to extend prior law through 2014. For facilities on which construction begins after 2014, the proposal would permanently extend the credit, make it refundable, and apply it to electricity consumed by the producer.

IMPACT. The PTC has numerous supporters, and many detractors, in Congress. President Obama's support for extending the PTC may encourage lawmakers, particularly in the Senate, to include the PTC in a tax extenders package.

Energy-Efficient Commercial Building Property. The FY 2015 budget would extend current law, which is used primarily for new buildings, through 2014. For facilities placed in service after 2014, the proposal would permanently extend and increase the deduction, and modify it to apply to energy savings from retrofitting existing commercial buildings.

COMMENT. The popular Code Sec. 25C residential energy property credit expired after 2013 and could be part of a tax extenders package. The Code Sec. 25D residential energy efficiency property credit is available through 2016.

Advanced Energy Projects. The President urged Congress to authorize an additional $2.5 billion of credits for investments in a qualifying advanced energy manufacturing project that establishes or enhances a manufacturing facility that produces clean fuels and energy related to electric vehicles, electric grids, electric drive motor vehicles, and other users of clean energy.

Clean Energy Vehicles. The FY 2015 budget would replace the existing credit for plug-in electric drive motor vehicles with a credit for advanced technology vehicles that operate on an alternative to petroleum. The credit would apply to vehicles placed in service after 2014 and before 2022. The FY 2015 budget also proposes a tax credit for medium-sized alternative-fuel commercial vehicles weighing between 14,000 and 26,000 pounds and heavy-duty alternative-fuel commercial vehicles over 26,000 pounds. This credit would expire after 2020.

Fossil Fuels. President Obama renewed his proposals to eliminate certain fossil fuel preferences for oil, natural gas, coal and other hard mineral fossil fuels. Affected provisions include enhanced oil recovery credits, marginal well credits, the deduction for intangible drilling costs, percentage depletion, the domestic manufacturing deduction (for oil and gas), and other incentives.

International Proposals

President Obama's FY 2015 budget proposals on international taxation seek to "level the playing field" so that multinational companies pay their "fair share" of U.S. taxes. The budget includes a number of new proposals to curb techniques that erode the U.S. tax base by limiting U.S. interest deductions, restricting "stateless" income, and tightening the rules on corporate inversions. The proposal also includes a number of measures from previous budgets that address income-shifting and other loopholes.

COMMENT. International tax avoidance, both outside of the law and technically within it, has been targeted by the Obama administration as a drain on the economy and a source of patent unfairness. The FY 2015 budget reflects the impact of the Organisation for Economic Cooperation and Development's (OECD) proposals on base erosion. Meanwhile, within the larger framework of tax reform, the debate continues in Congress over whether a territorial or worldwide tax system is better; and whether lower corporate tax rates, or the elimination of them entirely, will make the U.S. economy stronger.

New/Amended Proposals

Interest Expense Deductions. Under current law, multinational groups with a foreign parent "inappropriately" reduce their U.S. taxes on U.S. income by over-leveraging U.S. operations relative to their operations in lower-tax jurisdictions. The President proposed to address this practice, by limiting U.S. interest expense deductions to the amount of a U.S. financial reporting group's interest income, plus the U.S. group's proportionate share of the subgroup's net interest expense.

©2013 CCH Incorporated. All Rights Reserved.

IMPACT. "Interest-stripping" by claiming interest deductions is one of the simplest measures for eroding the tax base, according to Treasury. The President's proposals would restrict the amount of interest expense that U.S. and foreign multinationals can deduct against their U.S. operations.

COMMENT. This proposal is a companion to a 2014 budget proposal that would defer interest deductions for U.S. parented groups where income of a foreign subsidiary is also deferred.

Stateless Income. Some multinational groups have exploited inconsistencies between U.S. and foreign tax law to avoid paying taxes anywhere, creating "stateless income," according to Treasury. The FY 2015 budget would address these forms of tax arbitrage by limiting the use of hybrid entities, hybrid instruments and hybrid transfers to create stateless income. The proposal would deny U.S. deductions for interest or royalty payments to a related party where there is no corresponding income inclusion or there would be a duplicate deduction in both the U.S. and a foreign jurisdiction.

IMPACT. These provisions would broaden the U.S. tax base and increase revenues, Treasury predicted.

Digital Goods And Services. President Obama proposed to create a new category of subpart F income (foreign income that is taxed currently even if not repatriated to the U.S.). Foreign base company digital income would arise where a controlled foreign corporation (CFC) uses intangible property developed by a related party but does not make a substantial contribution to developing the property or services generating the income.

IMPACT. Existing categories of subpart F income do not adequately address mobile income earned from providing digital goods and services and allow CFCs to shift the income to low-tax jurisdictions, eroding the U.S. tax base, the administration explained. For example, a company may avoid U.S. taxes by licensing software to an off-shore affiliate in a low-tax jurisdiction, which then sells the product to consumers, rather than selling directly from the U.S. to consumers.

Other Subpart F Income. Another new proposal would address the avoidance of foreign base company sales income through the use of manufacturing services arrangements. The proposal would expand this category of income to include income of a CFC from the sale of property manufactured on behalf of the CFC by a related party.

Corporate Inversions. Current law attaches consequences to inversion transactions in which a U.S. corporation is replaced by a foreign corporation as parent of a worldwide group of companies. If the historic U.S. shareholders own 80 percent of the foreign parent, the transaction is disregarded for tax purposes. If the shareholders own 60 percent but less than 80 percent, the foreign status of the parent is respected, but other tax consequences apply. President Obama proposed to reduce the 80-percent ownership threshold to more-than-50-percent, and would eliminate the 60-percent threshold, for treating the inverted corporation as a U.S. company. An inversion transaction would also occur where, regardless of the level of shareholder continuity, the foreign corporation has substantial business activities in the U.S. and the foreign corporation is primarily managed and controlled in the U.S.

IMPACT. Existing law has not sufficiently discouraged inversion transactions, and there remains a significant potential for substantial erosion of the U.S. tax base, Treasury indicated.

Revenue raisers

Top revenue raisers in the FY 2015 budget (based on Green Book estimates) include*:

28 Percent Cap on Deductions and Credits	$598.1
Estate / Gift Tax at 2009 levels	$118.3
Repeal of LIFO	$82.7
Tobacco Tax Increase	$78.2
Foreign Tax Credit on Pooling Basis	$74.7
Expansion and Indexing of FUTA wage base	$59.0
Financial Crisis Responsibility Fee	$56.0
Buffett Rule / Fair Share Tax	$53.0

**In billions of dollars, over 10 years*

Note: Some proposals, lathough "high-profile," would only raise a limited amount of revenue. For example, $13.8B from taxing carried interest.

©2013 CCH Incorporated. All Rights Reserved.

Renewed Proposals

FATCA implementation. The President proposed to require U.S. financial institutions to report account balances for U.S. accounts held by foreign persons. A second proposal would expand reporting required for U.S. source income paid to accounts of foreign persons, to include similar non-U.S. source payments.

IMPACT. Under the Foreign Account Tax Compliance Act (FATCA), the U.S. is requiring foreign financial institutions and governments to provide information to the IRS on foreign accounts with U.S. owners. A foreign jurisdiction's willingness to share financial and tax information with the IRS often depends on the willingness of the U.S. to reciprocate by providing comparable information. Requiring U.S. financial institutions to report to the IRS the same information that is required under FATCA will facilitate these information exchanges and support foreign governments concerned about tax evasion by their residents.

COMMENT. The first proposal is also significant because it would affirm the IRS's authority to obtain information on accounts of foreign persons, even where the income is not subject to U.S. taxes. IRS regulations currently require this reporting, but the requirements are being challenged by the U.S. banking industry.

Other proposals. The President's FY 2015 budget also renewed several other proposals:

- Limit the shifting of income through intangible property transfers by expanding the definition of intangible property to include workforce in place, goodwill, going concern value, and other valuable items;
- Tax the gain from a sale of a partnership interest on a look-through basis; and
- Prevent the use of leveraged distributions from related corporations to avoid dividend treatment.

Tax Administration

The President's FY 2015 includes a large number of tax administration proposals affecting some filing deadlines, electronic filing, penalties, information reporting, return preparers, and more.

New/Amended Proposals

Return Dates. Calendar year partnership and calendar year S corporation returns (Form 1065 and Form 1120-S) along with Schedule K-1s provided to partners and shareholders would be due March 15. Returns of calendar year corporations other than S corporations would be due April 15 instead of March 15. Information returns would be required to be filed with the IRS or Social Security Administration by January 31; Form 1099-B would be required to be filed by February 15.

IMPACT. Calendar year S corporation filing deadlines would remain the same. Partnership filing deadlines would be made to conform to the deadlines for S corporations.

COMMENT. Similar proposals have been floated in the House Ways and Means Committee and the Senate Finance Committee. One version could be enacted as a standalong bill or added to another bill.

Math Error Authority. Under the President's proposal, the IRS's "math error" authority, which allows the agency to correct certain mistakes without performing an audit, would refer only to computational errors and the incorrect use of any tables provided by the IRS. However, a new category of "correctable errors" would be created.

IMPACT. The IRS would be authorized to correct errors in cases where the information provided by the taxpayer does not match the information in government databases; the taxpayer has exceeded the lifetime limit for claiming a deduction or credit; or the taxpayer has failed to include certain documentation with his or her return.

COMMENT. In recent years, the Treasury Inspector General for Tax Administration (TIGTA) has reported problems with tax-payers failing to provide the requisite documentation, such as for the adoption credit. The FY 2015 proposal builds on one made in the President's FY 2014 budget.

Return Preparers. President Obama proposed to clarify that the IRS has authority to regulate all paid tax return preparers.

IMPACT. The proposal would effectively reverse Loving, 2014-1 USTC ¶50,175, where the Court of Appeals for the District of Columbia Circuit struck down the IRS's registered tax return preparer (RTRP) program.

Preparer Penalties. The Code Sec. 6694(b) preparer penalty for understatements due to willful or reckless conduct would be enhanced. The Code Sec. 6695A penalty relating to appraisers of property value would be modified to institute a more administrable "reasonable cause" standard. In addition, the proposal would preclude an appraiser from being subject to both penalties for the same appraisal. The President also proposed to extend the preparer EITC due diligence rules to the child tax credit.

Return Information. The IRS would be authorized to disclose returns and return information to customs officials (Department of Homeland Security).

Shareholder Liability. The proposal would impose secondary liability on the corporation's shareholders (without regard to state law) for payment of an "applicable C corporation's" income taxes, up to the amount of sales proceeds received by shareholders selling a controlling interest in the corporation's stock. A corporation is an applicable C corporation if two-thirds of its assets consist of cash, passive investment assets, or other assets being sold.

©2013 CCH Incorporated. All Rights Reserved. Wolters Kluwer CCH

IMPACT. The transactions are structured so that the corporation's assets are sold after the stock transfer, and the corporation is left with insufficient assets to pay taxes from the asset sale. The stock price reflects the unpaid federal income tax. The proposal would enable the IRS to collect the unpaid taxes from the selling shareholders.

Renewed Proposals

E-filing. The President reproposed a number of changes to current e-filing rules. Individuals who prepare their income tax returns electronically but print them and file on paper would be required to include a scannable code. All corporations and partnerships with $10 million or more in assets would be required to file returns electronically under the President's proposal. Regardless of asset size, corporations with more than 10 shareholders and partnerships with more than 10 partners would also be required to file returns electronically.

Information Reporting. As in past budgets, President Obama proposed expanded information reporting. These proposals include requiring information reporting for private separate accounts of life insurance companies and modifying the reporting of tuition expenses and scholarships on Form 1098-T.

Penalties. The President's proposal would index all penalties for inflation.

Limitations Period. The President proposed to create an additional exception to the general three year limitations period for the assessment of tax liability from adjustments to state or local tax liability.

Identity Theft. The President proposed to add tax crimes to the Aggravated Identity Theft Statute and impose a civil penalty in tax identity theft cases.

COMMENT. The IRS has significantly boosted its resources for curbing tax related identity theft, particularly by improving its return processing filters. The IRS has also assigned roughly 3,000 employees to work identity theft cases.

More proposals. Additional tax administration proposals would:

- Remove the requirement for an initial offer in compromise to include a nonrefundable payment
- Authorize the IRS to absorb credit and debit card processing fees for certain payments
- Require taxpayer identification numbers (TINs) from certain contractors
- Clarify the liability of employee leasing companies for employment taxes
- Allow the IRS to issue guidance on worker classification
- Expand IRS levy authority for payments to Medicare providers with delinquent tax debts
- Require streamlined audit procedures for partnerships with 1,000 or more partners
- Expand IRS access to the National Directory of New Hires
- Protect tax whistleblowers from retaliation and make other changes
- Require mandatory e-filing for filers of Form 990 series returns
- Authorize the IRS to require e-filing of Form 8955-SSA
- Permit offset of federal refunds to collect state income tax regardless of tax-payer's residence
- Impose a penalty on failure to comply with e-file requirements
- Modify indexing to prevent deflationary adjustments
- Implement a program integrity cap statutory adjustment for tax administration
- Facilitate compliance with local jurisdictions
- Eliminate some TIGTA reviews
- Improve investigative disclosure statute
- Require truncated SSNs on Forms W-2

©2013 CCH Incorporated. All Rights Reserved.
Wolters Kluwer
CCH

Treasury/IRS Funding. President Obama requested nearly $12.5 billion to fund the IRS in FY 2015, reflecting almost a 10 percent increase from FY 2014. Enforcement would receive an additional $349 million and taxpayer services would receive an additional $161 million.

IMPACT. IRS Commissioner John Koskinen has warned that the number of audits will fall by approximately 100,000 this year because of budget cuts. In addition, he cautioned that customer service will be impaired. The IRS is answering approximately six out of 10 calls from the general public this filing season, according to agency officials. Tax professionals are also reporting delays in the IRS answering practitioner hotlines.

Indexing / CPI

Indexing. The President's Budget proposal would modify inflation adjustment provisions to prevent tax parameters from declining from the previous year, where the underlying price index falls.

IMPACT. Many items, including personal exemptions, standard deductions, and income tax rate brackets, are indexed for inflation. If price levels decline for the year, the tax provisions can become smaller, as long as they are no less than their base period values. Preventing tax parameters from falling would promote economic stability and prevent reductions in various tax benefits. When the economy had been skirting with deflation during the height of the 2008-2009 recession, the IRS just avoided having to make the decision over downward application of inflation adjustments. This provision would avoid the issue entirely.

Chained-CPI. The President removed for the FY 2015 Budget a controversial proposal to measure inflation for tax purposes using an alternative version of the Consumer Price Index (CPI), called the Chained Consumer Price Index (C-CPI-U), rather than the standard CPI. A chained-CPI would generally measure inflation at a slightly lower rate than the standard CPI.

©2013 CCH Incorporated.
All Rights Reserved.

Wolters Kluwer CCH

Freed Maxick is the brand under which Freed Maxick CPAs, P.C. provides services to its clients. Square logo, FreedMaxick, and "Trust Earned." are trademarks of Freed Maxick CPAs, P.C.

Trust earned.

FREEDMAXICK.COM