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July 13, 2012 – Mid-year brings no resolution to fate of Bush-era tax cuts, extenders and more

Hopes for a pre-election resolution to the fate of the Bush-era tax cuts, extenders and other tax incentives are quickly fading as summer approaches. This year is increasingly looking like a replay of 2010, the last time the Bush-era tax cuts were facing imminent expiration. The White House, the Democratic-controlled Senate and the GOP-controlled House all have different opinions on the fate of these tax incentives and negotiations, which have been few and far between, and have quickly bogged down. One solution, which is being talked about more and more, is a temporary extension of the tax cuts. While this would punt the issue to the next Congress, it does little to ease taxpayers' concerns about tax planning in a climate of constant uncertainty.

Bush-era tax cuts

Unless extended, the tax cuts in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) (as extended by the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010) will sunset after December 31, 2012. The list of expiring tax incentives is long and includes reduced individual income tax rates and capital gains/dividends tax rates; the $1,000 child tax credit; enhancements to the earned income tax credit (EIC); and much more.

On May 15, House Speaker John Boehner, R-Ohio, said that the House will vote before the November elections on legislation to extend the Bush-era tax cuts. Boehner gave no timetable for a vote. It is unclear at this time if the GOP plans to vote on making the Bush-era tax cuts permanent or merely to extend them one or two more years. Also unclear is whether or not any extension would be offset with revenue raisers elsewhere. Even if the House votes on the tax cuts, there is no guarantee the Senate will take them up.

Complicating matters is the federal budget deficit. After months of partisan wrangling last year, Congress passed the Budget Control Act of 2011 (BCA). The BCA imposes mandatory, across-the-board spending cuts through sequestration. The BCA's spending cuts are scheduled to take effect in 2013. The GOP wants to repeal the BCA and on May 10, the House approved legislation to effectively do that. The GOP bill has no chance of passage in the Democratic-controlled Senate. So the BCA remains, for now, law.

Few Capitol Hill observers expect Congress to take any meaningful action on the Bush-era tax cuts before the November elections. This leaves the fate of the Bush-era tax cuts to the lame duck Congress. Depending on the outcome of the November elections, the lame duck Congress could do nothing and allow the Bush-era tax cuts to expire, make the tax cuts permanent, or--and this appears to be the most likely scenario--extend the tax cuts for one year. Either way, the uncertainty complicates tax planning for 2012 and beyond.

Small businesses

Lawmakers are also dueling over competing small business tax bills. The House has approved the GOP-sponsored Small Business Tax Cut Act. The GOP bill would, among other provisions, provide a deduction for 20 percent of qualified domestic business income of the taxpayer for the tax year, subject to limitations. In the Senate, the Democrats' small business bill would give a 10 percent income tax credit to small employers that increase wages or create jobs in 2012 and extend 100 percent bonus depreciation through 2012 (which had expired at the end of 2011). If the Senate approves the Democratic bill, the two chambers could iron-out the differences in the bills in conference.

Tax extenders

Since January, supporters of the tax extenders have tried several times, all unsuccessfully, to attach the extenders to other bills. Some of the extenders were initially attached to the Middle Class Tax Relief and Job Creation Act of 2012, which extended the employee-side payroll tax cut for all of calendar year 2012, but were subsequently dropped. Supporters also tried to include many of the extenders, especially energy-related tax incentives, to the Senate's highway funding bill: the Moving Ahead for Progress in the 21st Century (MAP-21) Act. At the last minute, the extenders were removed from the Senate bill.

A drag on the extenders is their estimated cost to the federal budget. According to the Congressional Research Service, renewing all of the extenders for 2012 would cost $35 billion. This is one reason why supporters have tried to move only some of the extenders. There have also been calls in Congress to let some of the extenders expire permanently; but every extender has its supporter.

Federal estate tax

Another big question mark hovers over the federal estate tax. Unless Congress acts, the federal estate tax is schedule to revert to its pre-EGTRRA levels (a top tax rate of 55 percent with a $1 million exclusion). In 2010, the White House and the GOP agreed on a top tax rate of 35 percent with a $5 million exclusion (indexed for inflation) for decedents dying in 2011 and 2012 (special rules applied to decedents dying in 2010). The GOP has proposed to eliminate the estate tax entirely or, if not abolished, to retain the 35/$5 million amounts for decedents dying after 2012; the White House has proposed to reduce the exclusion amount to $3.5 million.