SMALL BUSINESS LEGISLATIVE COUNCIL

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RE-LAUNCH

The campaign to repeal the infamous "Form 1099" expansion begins anew. In the House, Representative Dan Lungren (R-CA) has introduced H.R. 4, the Small Business Paperwork Mandate Elimination Act of 2011, legislation to repeal the expanded tax information reporting requirement established by the health care reform law. He has 245 co-sponsors.

The expansion provision was inserted into the health care reform legislation, even though it has nothing to do with health care, as a revenue offset. The last Congress was required to "pay for" any increase in spending or reduction in tax revenues with offsetting decreases in spending or revenue increases elsewhere. The Form 1099 provision, which refers to the Internal Revenue Service (IRS) form number, was projected to raise $17 billion.

Under existing tax law, a business taxpayer making payments to a service provider (the "payee" in IRS language) aggregating to $600 or more for services in the course of a trade or business in a year is required to send an information return to the IRS (and to the service provider-payee) setting forth the amount, as well as name and address of the recipient of the payment (generally on Form 1099). Under the law, the business taxpayer is not required to issue a Form 1099 to a corporation that provides services to it.

The new law made two changes. The first was to require businesses to issue the Forms 1099 to corporations as well as all persons in a trade or business. The second was to expand significantly the scope by requiring the issuance for payments made to "property" providers as well as service providers. The provision is effective for payments made after December 31, 2011. The existing threshold of $600 or more in payments remains as is.

The $600 or more in payments is now for "rent, salaries, wages, amounts in consideration for property, premiums, annuities, compensations, remunerations, emoluments, gross receipts or other fixed or determinable gains, profits and income…" The business taxpayer that issues the Form 1099 must first obtain the Taxpayer Identification Number (TIN) of the service/property provider-payee. If the service/property provider-payee does not provide the TIN to the business taxpayer, the business taxpayer must "backup" withhold from the payments at a 28 percent rate.

The payments that are included under the expanded scope are not only those made directly by check but also those made by other means such as credit cards, for example. Think about the airlines, hotels, rental cars, and restaurants that appear on your credit card bill. You might not think of them as vendors of goods and services, but that is what they are. Also, if you are in the business of selling or distributing goods, all of your suppliers of products are also vendors under the new law. (Under existing law there are regulations that provide narrow exceptions for some types of vendors (telegrams, telephone, freight, storage) and some individual vendors that accept payment from you by credit card and meet qualifications set forth by the IRS. Even if some regulatory exceptions are carried over under the new law, you will still be the one responsible and liable for issuing the information report and it will not be easy to sort it out.)

And, of course, any business that pays you more than $600 will be sending you a Form 1099.

A separate new law has increased the penalties if the business taxpayer fails to file the information return with correct information. The penalty is:

- *$30 per information return if you correctly file within 30 days (by March 30 if the due date is February 28); maximum penalty is $250,000 per year ($75,000 for small businesses)*
- *$60 per information return if you correctly file more than 30 days after the due date but by August 1; maximum penalty is $500,000 per year ($200,000 for small businesses)*
- *$100 per information return if you file after August 1 or you do not file required information returns; maximum penalty is $1,500,000 per year ($500,000 for small businesses)*

The definition of small business for the purpose of calculating penalties only is average annual gross receipts of $5 million or less for the three most recent tax years (or for the period a business has been in existence, if shorter) ending before the calendar year in which the information returns were due. The new penalties are effective January 1, 2011. There are no plans to repeal the penalty increases but they present just one more reason to repeal the expansion.

Senator Mike Johanns (R-NE) plans to introduce his Form 1099 repeal bill when the Senate returns next week.

The question is whether the Democrats are forced to eat the whole humble pie. At the end of the last Congress, the Democrats wanted to repeal the provision without offsetting the revenue that the provision was designed to produce to pay for part of the health care bill. In this Congress, the House can pass a repeal bill without a revenue offset. It changed its procedural rules to no longer require "paygo" offsets. In the Senate, an offset is needed by their rules and the legislation must ultimately be accounted for under the statutory paygo law The massive Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act, passed last year seemed to be the ideal vehicle for repeal, since Congress was declaring an emergency under the statutory paygo law, to waive paygo requirements. The political reality was and is that the Republicans do not want to let the President and the Democrats off the hook for the responsibility for paying for health care reform.

SBLC maintains a simple open access site for small businesses to use to urge Congress to repeal the provision. It is www.stopform1099.org

PAYGO PRIMER

I am going to try to explain the story behind statutory paygo and the 112th Congress. I have the feeling I am going to have to refer to it many times over the next two years, and it will be a lot easier to say "See the 01-17-11 Weekly."

By now, I am hoping everybody understands the general principle behind "paygo." The idea is that any time Congress wants to increase mandatory spending or reduce tax revenues (i.e. tax relief), it should decrease spending or increase tax revenues elsewhere in order not to incur a federal deficit (i.e. tax revenues do not match spending). We could have a long debate about the general concept. I happen to believe low taxes lead to economic activity which ultimately leads to more tax revenue. On the other hand, as an ardent believer in fiscal responsibility, I have concluded that we have to deal with federal deficits in real time rather than within extended time frames.

For a number of years, Congress has been operating under paygo rules. These are internal rules, not laws. In February, 2010, it decided to place a law on the books to impose a "statutory" paygo requirement. That law, as I will explain, does not operate along the same lines as congressional rules. Redundant to some extent, but the theory was that it is harder to break a law than rules. Procedurally, one could pass a law that meets the paygo rules of the Senate or House but not the paygo law.

In the 111th Congress, the Senate and House both operated under similar paygo rules. In the 112th Congress, the two chambers will operate under very different rules. Since most Congresses, Democratic or Republican led, had a hard time with the concept of decreasing spending, such paygo options were seldom used. The more common paygo compliance option was to increase tax revenues. The phrase "revenue offset" is frequently used.

Under the cloak of rhetoric, these have been referred to as "loophole closing" or tax gap compliance. As the late Senator Russell Long said years ago, "Don't tax me, tax that guy behind the tree." (Technically he was talking about tax reform and that is another story for another day), but you get the idea. The Form 1099 expansion will go down into history as a revenue offset that spiraled out of the realm of common sense.

The Senate will continue with rules that require either a spending decrease or a revenue offset. (There are ways to get around the rule; in the Senate, a motion to waive that is approved by 60 Senators will do it). Under its new rules, the House will require spending decreases to offset spending increases, but tax revenue offsets will not be required for tax relief.

So now we come to the statutory paygo requirement. Congress can pass individual bills that do not meet paygo principles and not immediately run afoul of the statutory paygo requirement. (I guarantee this is the nuance that is going to have me including "See 1-17-11 Weekly" in articles.) That is because the enforcement mechanism under statutory paygo delays the day of reckoning. If Congress enacts bills cutting taxes or increasing mandatory expenditures without fully offsetting the costs, the PAYGO law specifies a penalty, called "sequestration" that kicks in at the end of a congressional session.

Under the PAYGO law, the Office of Management and Budget (OMB) must maintain both a five-year and a 10-year PAYGO scorecard. One scorecard displays the costs or savings produced by legislation averaged over the first five years, and a second scorecard with the costs or savings averaged over the first 10 years. The costs or savings of every bill enacted from February 12, 2010, onwards will be recorded on the scorecards. At the end of each session of Congress, the OMB will add all the (averaged) costs and savings for the fiscal year that has just started, to determine whether a sequestration is necessary.

If Congress adjourns at the end of a session with net costs – that is, more costs than savings - on the scorecard, the OMB is required to calculate, and the President is required to issue a sequestration order implementing, across-the-board cuts to a select group of mandatory programs in an amount sufficient to offset the net costs on the PAYGO scorecard.

Now there are other ways to "get around" statutory paygo (and it so happens that is what Congress did when passing the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act (TRUIRJCA), at the end of 2010):

* Off-budget costs or savings are excluded. The Social Security trust funds and the Postal Service fund are the only two federal programs designated as off-budget by law. If legislation affects Social Security, for example, those effects, though shown in the unified budget, will not be entered on the PAYGO scorecards.

* Emergency costs are excluded. If Congress statutorily designates specified costs as emergency requirements under the PAYGO law, the costs are not entered on the PAYGO scorecard but instead are shown separately. (This is the huge loophole through which much of TRUIRJCA got around statutory paygo.)

* Certain timing shifts are excluded. Congress cannot use timing shifts to avoid violating PAYGO on the 10-year scorecard. If a bill contains provisions that would move costs from year ten of the scorecard to year 11, or would move savings from year 11 onto the last year of the scorecard, the effects of those timing shifts are ignored.

* CLASS Act savings are excluded. The CLASS Act, enacted as part of health care reform, established a voluntary, fully prefunded long-term care benefit, with the value of the benefit linked directly to the value of the advance funding. Because it is fully prefunded, the legislation reduces deficits in the early years but over time breaks even. A special provision of the PAYGO law provides that the CLASS Act does not have its budgetary effects entered on the PAYGO scorecard.

* Current-policy scorekeeping adjustments can reduce scored costs for certain specific exceptions to the PAYGO law that were included in the law:

1. Some longstanding programs require periodic reauthorization, such as farm price supports, SNAP (food stamps), the Children's Health Insurance Program (CHIP), and Temporary Assistance to Needy Families (TANF). These programs are treated as though they are ongoing. This has been the baseline rule since baselines were first developed in the 1970s.

2. Alternative Minimum Tax. The PAYGO law provides that legislation extending relief from the scheduled Alternative Minimum Tax (AMT) hit is not scored as producing PAYGO costs except to the extent that the relief is more generous than the relief currently in effect. The PAYGO law provides for these downward current policy adjustments only for AMT relief through December 31, 2011. (Used in part for scoring TRUIRJCA for statutory paygo purposes)

3. Reimbursement rates for Medicare physicians. The benchmark for the current policy adjustment is the physician reimbursement rates as they were in effect in 2009, and the adjustment in scoring is done in the same way as that for the AMT. This adjustment only offsets the costs of a fix to this payment system through December 31, 2014.

4. Estate Tax Relief. Tithe benchmark for the current policy adjustment is the estate and gift tax law as it was in effect for 2009, and the scoring adjustment method is the same as for the AMT. This adjustment only offsets the costs of revisions to estate tax law in place through December 31, 2011. (Used in part for scoring TRUIRJCA for statutory paygo purposes.)

5. Individual Tax Relief A wide variety of cuts to the individual income tax were enacted in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). The benchmark for the current policy adjustment is the relevant provision of the tax code as in effect for 2010, and the scoring adjustment method is the same as for the AMT. However, this relief does not apply to all the provisions of EGTRRA and JGTRRA – only those referred to as the middle-class tax cuts. (Used in part for scoring TRUIRJCA for statutory paygo purposes). If the upper-income tax cuts are to be extended, their extension must be paid for. Under the PAYGO law, permanent current policy adjustments are allowed for the following provisions of EGTRRA and JGTRRA:

*The 10-percent income tax bracket;
*The child tax credit;
*Tax benefits for married couples;
*he adoption tax credit;
*The dependent care tax credit;
*The employer-provided child care tax credit;
*The education tax benefits;
*The 25-percent and 28-percent tax brackets;
*The 33-percent tax bracket, but only for taxpayers with Adjusted Gross Income (AGI) of $200,000 or less for single filers or $250,000 or less for married filers;
*The tax rates on capital gains and dividends, but only for taxpayers with AGI of $200,000 or less for single filers or $250,000 or less for married filers;

*The phase-out of personal exemptions (PEP) and the limitation on itemized deductions (Pease), but only for taxpayers with AGI of $200,000 or less for single filers or $250,000 or less for married filers; and
*The increased limits on "expensing" small business assets under §179(b) of the Internal Revenue Code.

As described in items two through five above, current policy adjustments allow the enactment without offsets of relief from certain scheduled changes in laws. Whether the relief is allowed through 2011 (AMT, estate tax), through 2014 (Medicare physician reimbursement rates), or permanently (middle-class tax cuts), the legislation providing that relief must be enacted by December 31, 2011, to be eligible for the current policy adjustments.

There is one more way around the statutory paygo – dealing with the original cost estimates. The PAYGO law provides two mechanisms for providing PAYGO cost estimates. The first uses an estimate included in the Congressional Record by the Chairs of the Budget Committees. The second relies on OMB to produce the PAYGO estimate.

Under the first mechanism, Congress can determine the costs or savings of legislation for purposes of the PAYGO law by enacting those estimates into law. Under the PAYGO law, Congress would include within the text of a bill a cross-reference to an estimate that will have been included in the Congressional Record by the Chairs of the Budget Committees. That estimate must be submitted to the Record before the House of Representatives or the Senate has voted on final passage of that bill but after they have voted on the last amendment (if any) to that bill.

In the House's newly adopted rules, their Budget Committee Chair, Paul Ryan (R-WI) has been given new authority on behalf of the House to exempt from estimates the budgetary effects of the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Jobs and Growth Tax Relief Reconciliation Act of 2003. It also exempts the budgetary effects of the repeal of the Patient Protection and Affordable Care Act and Education Affordability Reconciliation Act of 2010. The budgetary effects of AMT relief, estate tax, trade agreements and small business tax relief are also exempted. The exemption is limited to measures which do not increase the deficit or revenues over the ten-year budget window, except for increases in revenue which meet certain specific criteria.

But here's the catch: The two chambers' Budget Committee Chairs have to agree when it comes to a final bill whether it is a conference report or an amendment to a version passed by the other chamber. The operative words are they have to "jointly submit" the estimates for printing in the Congressional Record. With a Republican in the House and a Democrat in the Senate, good luck with that.

The general media has its way of reducing this whole thing to a simple sound bite or paragraph. For SBLC, when I have to write about revenue offsets and the dynamics of a particularly initiative, I am just going to go with "See the 01-17-11 Weekly."

SBLC ANNUAL MEETING

The SBLC annual meeting will be held on Thursday, February 10, 2011 at the Grand Hyatt Hotel at 1000 H Street, NW in DC.

The meeting will begin at 8 a.m. and end at 10 a.m. Breakfast will be served.

Registration forms have been sent.