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TRUE UP

I know you are as tired of reading about Form 1099 as I am of writing about it. It astounds me how much time Congress has wasted on this discussion.

The House has passed H.R. 4, the bill to repeal the Form 1099 expansion. Before approving the bill, the House substituted the language of H.R. 705, the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011. As a result, the bill now includes a repeal of an additional Form 1099 expansion that was included in another law late last year, and the bill would offset the cost of both repeals with a reduction in a subsidy for premium payments under the new health care law.

The other expansion of the Form 1099 requirement was added by the Small Business Jobs Act in September, 2010. Under prior law, recipients of rental income from real estate who are not otherwise considered to be engaged in a trade or business of renting property were not subject to the same information reporting requirements as taxpayers who are considered to be engaged in

a trade or business. The expansion requires these "incidental" rental income recipients making payments of \$600 or more to service providers that provide services for the rental property to issue Form 1099s to those service providers (e.g. cleaning service, maintenance).

There was a spirited debate regarding the nature of the offset, with the Republicans forced to defend the offset as not being a tax increase even though it generates the revenues necessary for the offset. The term they used to describe the offset is that it is a "true up." I am going to take another stab at explaining it. Most Republicans have taken an anti-tax increase pledge and for better or worse, it results in some tortured rhetoric on both sides of the aisle.

It starts with the fact that last year's health care reform law provides premium purchase assistance based on a person's or family's income. The premium assistance credit, which is refundable and payable in advance from the government directly to the insurer, will subsidize the purchase of certain health insurance plans through a State exchange (when the system is up and running). The premium assistance credit will be available

for single or joint filers with household incomes between 100 and 400 percent of the Federal poverty level ("FPL") for the family size involved who do not receive health insurance through an employer or a spouse's employer.

The complicated part of the premium assistance is the method for determining what the amount should be. During each year's open enrollment period for coverage, exchange participants must provide information from their tax return from two years prior. This is going to create situations in which the premium assistance credit provided is going to be more than what the later tax return for the actual year demonstrates what should have been the correct amount.

Congress recognized it had a problem soon after it passed the health care reform law. A law enacted late in 2010 imposed a recapture mechanism for the extra assistance but with limitations on how much can be recaptured.

Under that initial version of a recapture rule, the excess advance payment basically shows up as additional income on the taxpayer's income tax return for the taxable year. When Congress passed the

recapture law, it recognized it would be difficult to be precise so it used brackets for the recapture amounts and softened a “cliff” for the top level. Remember, the odd part is that the taxpayer does not actually receive the premium assistance. The payment from the government goes directly to the insurer so when the recaptured excess amount is reported on tax returns as income, there are going to be a lot of unhappy people since no cash actually ever passed through their hands. (Yes, I know. Some of you are thinking this is yet another example of why this health care reform isn’t such a good idea to begin with.)

While there was some talk about preventing fraud, the bulk of excess recaptures are going to be the result of the fact a taxpayer’s income happened to go up and thus the credit advanced was more than it should have been. Inadvertent tax liability.

Also, all of this is still hypothetical, since the premium assistance does not start until 2014.

The offset passed by the House would compress the “brackets” of the limitations on the liability recapture, so that higher eligible income brackets have more of the “excess” assistance recaptured. In effect, it makes the recapture more precise. The Democrats argued the provision is a tax increase for those taxpayers. The Republicans argued that it was just a “true up” to make sure that the spending provided by the government provided was no more than what was permitted by law.

Now it is up to the Senate to decide what to do. The easy thing would be to pass the House passed bill and send it on to the President for signature. But nothing is ever easy in the Senate and it does not appear that is the majority’s preference. There are three other options. All three of which would result in the bill being returned to the House and it would then have the options to pass the Senate version or go to conference.

The Senate could strip out the revenue offset. To do this, it would have to waive its offset rule to pass the bill without an offset, something it is not likely to do.

The next option would be to amend the House bill to substitute the offset passed by the Senate in the FAA bill. The offset is a rescission of unspent funds. The last option is that the Senate Democrats could come up with a revenue offset option acceptable to the Senate Republicans. The current rumor is that it is the option the leadership is pursuing.

The bottom line is we still have a ways to go.

PATENT REFORM

The Senate is expected to finish up its debate on patent reform. During last week’s debate, the proponents rebuffed an effort to retain the current “first to invent” patent grant. The pending bill provides for “first to file” patent rights. The “first to invent” priority has long been considered advantageous to small businesses without the resources to get to the patent office first.

The Senate has jettisoned many of the damage provisions in the Judiciary Committee-reported bill. The reason given is that the court with principal jurisdiction over patent litigation has cleaned up many of the problems through precedents.