



SBLC WEEKLY

September 6, 2011

Volume XIII, Issue 33

THE COMMITTEE OF TWELVE

Anointed by their leaders, the six Senators and six Representatives tasked with the duty of finding between \$1.2 trillion and \$1.5 trillion in deficit reduction recommendations will begin their work in earnest this month. If they fail to agree on recommendations, the federal government will face a haircut across the board. The process of automatic cuts is known as “sequestration.”

If the Committee of Twelve can agree on recommendations, there is not much between their divine inspiration and enactment. The rest of Congress will largely be bystanders as the recommendations are only subject to “up or down” votes and most procedural obstacles have been waived as part of the law that created the Committee of Twelve.

From a human dynamic aspect, the telling element of the structure is the fact the recommendations require only a majority vote of the Committee. Only in Washington is the fact, “*only* a majority” a significant fact. With sequestration looming if they fail, one could probably make an argument that the Democrats have a slight advantage.

How much worse off would their favored programs be under sequestration than if one of them signs off on a deal that is comprised solely of spending cuts? For the Republicans, the pressure is all about taxes. Is one of the Republican six willing to take the leap? Seems to me, if one Republican is going to jump, he is going to want it to be at least a twosome. Favored Republican programs probably suffer more under sequestration but is sequestration worse than revenue increases? No easy answers.

The range of possibilities before the Committee of Twelve is vast. Putting aside the revenue scoring semantics, their ability to secure the \$1.2 trillion to \$1.5 trillion could include not only some revenue increases but also some “stimulus” revenue relief and/or spending increases. If they reach the top line (with the appropriate scoring), what lies below the surface can be creative.

Ramifications for small business – Sequestration is likely to hit small business harder than a deal. While not all small businesses utilize SBA programs, automatic cuts would pare it to the bone. Even for programs favored by all small

businesses, such as the Office of Advocacy, it would be hard blow. One would assume a deal would treat small business with gentler hands.

We have worried about tax reform. While inclusion in a deficit reduction seems like a remote possibility, it cannot be ruled out. The concern is who are the winners and losers under a tax reform package? Previous discussions have favored throwing out deductions and credits for all businesses but providing the rate relief to C Corporations only.

Revenue increases without reform (e.g., ethanol credit, corporate jets) would likely hit sectors rather than across the board so the impact on small business would not be significant unless something like LIFO repeal was to surface again.

Then you have the oddly curious potential outcomes. Republicans have argued that the scoring baseline includes assumptions that the so called Bush tax cuts (marginal top rate, estate tax relief) would expire. From the deficit reduction standpoint, this is considered good news because if it is true, the Democrats do not gain any revenue for deficit reduction for

the purposes of this exercise. But where does this leave us in the post Committee of Twelve world? Having made the argument that it has been assumed they would expire, how do you argue next year, that you cannot let them expire without having to face "But you already have conceded they need to expire for deficit reduction." Regardless of the semantics, it would be great to get permanent resolution of those two issues as part of package. (For example, continue the current estate tax relief structure as is, and let the top marginal individual rate rise only for incomes over a certain amount (\$5 million?).)

REGULATIONS

We expect a few new regulations to be released soon. The National Labor Relations Board's chair's term expired during August and we got a new poster for the bulletin board. The Democrats still hold a 2-1 majority. However, they lose another at the end of the year so look for the union election process rules to be finalized.

The Consumer Product Safety Commission (CPSC) will lose a Democratic commissioner in October. At that point, it will become a 2-2 commission.

I think I can say with some degree of confidence that Senate minority is not about to let the Senate approve any new appointees to regulatory agencies in the near future. The Senate minority has also been particularly adept at keeping the Senate in session during recesses to prevent any temporary recess appointments.

We are still awaiting the Department of Transportation's Hours of Service rule for truck drivers. It had been postponed when the department released some new data but it is under court order to finish the project up.

GOVERNMENT CONTRACTOR WITHHOLDING

The House is expected to vote on legislation to repeal the first of the tax gap measures that worked its way into law several years ago. The three percent withholding provision was imposed by the Tax Increase Prevention and Reconciliation Act of 2005. It imposed a requirement on Federal, state, and local governments to withhold taxes from government contractors beginning in 2011.

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act as Public Law 111-5. The law delayed the effective date of the withholding requirement by one year to 2012.

The Internal Revenue Service earlier this year announced it is delaying implementation until 2013. Withholding and reporting requirements will apply to payments made after December 31, 2012. In addition, payments made under contracts existing on December 31, 2012, that are not materially modified, will be exempt until January 1, 2014.

The House bill is H.R.674, introduced by Representative Wally Herger (R-CA).

PATENT SYSTEM REFORM

It appears the Senate will recede to the House's version of patent system reform. The bill changes our system from "first to invent" to "first to file" rights to a patent. The bill also establishes the opportunity for third parties to submit information (prior art) related to a pending application for consideration by a patent examiner in an effort to block the granting of a patent. The bill also creates a "first window" post-grant opposition proceeding, open for a period of time after the grant of the patent, to provide others an "easier" path to assert a patent should not have been granted. The theory is that an administrative challenge is "cheaper" than litigation.

The bill would prohibit patents on tax strategies. Current patent policy on tax strategies allows clever folks who come up with a good, legal way to reduce tax liability to charge you a fee if you use their clever idea.

The bill creates a transition program for review of business method patents, which have been controversial, as many alleged infringers claim that there is plenty of prior art on these methods and the patents should not have been granted. Business method patents claim "a method or corresponding apparatus for performing data processing operations utilized in the practice, administration, or management of a financial product or service, except that the term shall not include patents for technological inventions."

STIMULI

Under the bill, subject to available resources, the USPTO may establish a Patent Ombudsman Program. The duties of the program's staff shall include providing support and services relating to patent filings to small business concerns.

Under current law, small businesses receive a break on filing fees. They would continue to get such relief, while micro businesses would get a new additional reduction. The fees for maintaining patent applications and patents are reduced by 50 percent for small entities. Under the bill, the fees shall be reduced by 75 percent for micro entities.

A small business is defined on an industry by industry basis using the size standards published by the U.S. Small Business Administration. A micro entity is a small entity that has not been named on 5 or more previously filed patent applications and did not in the prior calendar year have a gross income exceeding 3 times the most recently reported median household income, as reported by the Bureau of Census.

There will be an effort to make a couple of changes (e.g. control of patent office fees) in the House bill on the Senate floor. The proponents of those changes will have to overcome the higher procedural obstacles to secure changes so their changes are modest.

If the Committee of Twelve does not do something to improve the state of the economy, I gotta believe Congress and the President will have to do so outside the parameters of the deficit reduction effort. I have not talked to too many small business owners who have had a good two or three months.

The President will offer a plan later this week.

There is some talk of a revival of the payroll tax relief for employers that hire new employees.

There is also talk of an extension of the current temporary payroll tax break for employees.

Doing something with regard to infrastructure spending is also a popular topic. This would be in addition to reauthorizations of the highway and aviation programs with which Congress has struggled.

The House majority will try to set a tone for easing the throttle on the regulatory engine with several regulations repeal efforts in its queue. Regulatory anxiety has become part of the cold water mix dampening business' economic enthusiasm.

While there may be a growing consensus on the need for more action on the economy, the problem is finding bi-partisan ground. The first thing anyone does in Washington these days is immediately brand any suggestion with a partisan label – regardless of its merits.

FISCAL YEAR

Oh by the way, guess what is coming in less than a month – the next fiscal year for the federal government, and guess what Congress will not have done again – fund the government on time.

I have not quite figured out how the appropriations process plays out with the on-going deficit reduction talks. But as I understand it, the appropriators have a pretty good idea of where they need to end up.

At this point, I would assume we are going to see a temporary continuing resolution (CR) to fund the government at least until the Committee of Twelve finishes (or does not finish) its work. I am sure there will be some unhappy campers about voting for any continuing resolution but I think they will be hard pressed to convince their colleagues – so I do not expect any sidebar spending reduction deals as part of the CR process.