SMALL BUSINESS LEGISLATIVE COUNCIL

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SPRING TIME IN WASHINGTON

The cherry blossoms blossomed over the weekend, after a slight delay due to chilly temperatures. Is the relationship between the Administration and the Republicans in Congress ready to warm up too?

The President will release his proposed budget for the federal government for fiscal year 2014 on Wednesday, (juuust a couple of months late). One could make the comment "Washington is always out of synch" when it comes to budget matters, but this year it is particularly so. "Normally," the first step is for the President to send his proposed budget to Congress. "Normally," they ignore it. "Normally," Congress tries and fails to pass a concurrent budget resolution. This year, the Senate and House have each passed their own versions of a budget resolution already. This year, the President's proposed budget may have some relevance to the process if the two chambers end up agreeing on a concurrent budget resolution. Go figure.

The President is supposed to present his proposed budget by the first Monday in February although there is no consequence if he does not. Congress is not obligated to consider it and seldom does. Also, since a concurrent budget resolution is an internal Congress action, it does not require a presidential signature to be binding on Congress.

In theory, Congress is supposed to pass a concurrent budget resolution by April 15th. Congress does not have to adopt a budget resolution and can proceed to the appropriations part of the process of funding the government for the upcoming fiscal year without one (six times since 1999). In the years it does not do so, Congress relies on the budget projections from the most recently passed version of a concurrent budget resolution for its appropriations efforts. If Congress does agree on a concurrent budget resolution, they do get to do some interesting things (if they choose to do so), one of which is "reconciliation." It allows certain budgetary items (primarily tax items) to move through the Senate process without filibusters (there are still some other parliamentary issues which require a supermajority in the Senate.)

Soooo. In May, there is a good chance the federal government will run up against its debt ceiling – technically. The government does have its now well-known bag of sleight of hand accounting tricks to delay default. Where am I going with this? Wouldn't it be weird if Congress does agree to a concurrent budget resolution, that the President's late proposed budget provides the framework for a compromise for a budget/debt reduction/debt ceiling deal, the impact of sequestration is mitigated, a long term debt reduction plan is put in place and tax reform under a reconciliation instruction process with a deadline happens? Okay, call me an optimist. But hey, the cherry blossoms are out.

Immigration reform is expected to bud sometime soon too. The so-called "gang of eight" in the Senate is slated to release their legislative proposal soon. For most small businesses, the principal issue will be the eligible-to-be-hired verification process. The proposal is expected to tighten up the penalties for hiring an illegal alien but also provide a more robust and timely document verification system.

PRESIDENT'S PROPOSED BUDGET

The Administration has been leaking an unusually large amount of information about the President's budget. We know that it includes most of the elements of the debt reduction plan the President offered to House Speaker John Boehner (R-OH) last year, thus it includes some entitlement reform, some other spending cuts and some increases in tax revenues.

On the revenue side, it appears the big-ticket item will be a limitation on the ability of high-income individuals to deduct various expenses. They would be able to deduct only 28 percent of those expenses. It does not appear the budget will specify which deductions would be subject to the limitation but you can be sure that the housing industry and charities are concerned.

In the parlance of the Bowles-Simpson proposal, these are known as "tax expenditures." Tax expenditures are defined under the Congressional Budget and Impoundment Control Act of 1974 as "revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."

What are the largest tax expenditures? According to the Tax Policy Center (for 2008 in $billions):

Exclusion of employer contributions for medical insurance premiums and medical care	$131
Net exclusion of pension contributions and earnings	117.7
Deductibility of mortgage interest on owner occupied homes	88.5
Accelerated depreciation of machinery and equipment	55.9
Deductibility of nonbusiness state and local taxes other than for owner occupied homes	49.1
Deductibility of charitable contributions	31.5
Deferral of income from controlled foreign corporations	30
Deductibility of state local property tax on owner occupied homes	29.1
Child credit	28.4

There apparently will also be a proposal to restrict how much you can accumulate in tax-deferred retirement accounts. You may be limited to $3 million in those accounts.

CHAINED CPI

One of the entitlement reforms will be a change to the inflation indexing methodology. One of the items under discussion is changing the type of Consumer Price Index (CPI) (yes, there is more than one) that is used for various federal benefit programs like Social Security. The idea is based on the belief the current CPI that is used does not reflect real world economic behavior and is thus too generous.

The index currently in use is the Consumer Price Index for All Urban Consumers (CPI-U). It measured the average change over time in the prices paid by urban consumers for a "market basket" of consumer goods and services. One of the other indices is the Chained Consumer Price Index for All Urban Consumers (C-CPI-U). The "regular" CPI uses a static basket of goods; the "chained" one reflects the effect of any substitution that consumers make across item categories in response to changes in relative prices. (The Administration will dress it up with a different name other than "chained.") The common example is that when the price of beef goes up, consumers switch to chicken if it is cheaper. So if you have a static basket of goods, you are not capturing the adjustment we make in the real world when prices go up.

There are a variety of other plusses and minuses for small business if there is a switch. The wage base for the social security portion of the FICA taxes is capped. The cap is tied to the CPI. If wage base grew less quickly, that would be a good thing (In fact, it has not gone up for two years). Income tax brackets are tied to the CPI as well.

Some of the provisions that allow small business owners to contribute to their pensions are also tied to CPI. They too have been flat, and if the logic of changing the CPI holds true, future increases would be less.

EMPLOYEE CHOICE - HEALTH CARE REFORM STYLE

Recently, there have been a proposal and some actions by the federal government to delay a couple aspects of the health care reform system that, in my view, are among the more interesting features for small businesses. Health care exchanges are to include an "employee choice" option for small employers. Under this option, the small business could say "I am paying a specific dollar amount for every employee," the employer chooses a metal tier, and the employee can choose whatever plan the employee likes within that metal tier. It is a sort of a "defined contribution" approach to health care benefits. Along with the employee choice feature, the exchanges will offer a premium aggregation feature that would allow the small employer to just write one check for its contributions and any amounts it withholds from employees' checks for their contributions.

As the result of one recent final rule, the federally-operated exchanges will not offer this option until 2015. At the moment, it looks like the federally-operated exchange will be "default" exchange, at least initially, in 33 states. The federal government has also just proposed allowing the state-operated exchanges to not offer the employee choice option in 2014. In 2015, all exchanges will have to offer this option. The reason is that the insurers and exchanges say they cannot get organized to handle this option in 2014.

Some say that the employee choice option, as opposed to having all the employees on the same plan, is going to raise rates across the board and there is probably some truth to that. But my gut says that the "employee choice" option is an attractive way for small employers that do choose to offer coverage to their employees, to get the business out of the middle of the "what is the best plan for all of us" decision making. I think that outweighs any downside to the overall cost of health care. In the short run, for those small employers currently not offering coverage, the delay of the employee choice option may be among the reasons not to start in 2014.

For those of you asking what are these "metal" tiers, here is the explanation. By 2015, it is going to be "common knowledge." ☺

Beginning in 2014, non-grandfathered health plans in the individual and small group markets must meet certain Actuarial Values (AVs), or metal levels: 60 percent for a bronze plan, 70 percent for a silver plan, 80 percent for a gold plan, and 90 percent for a platinum plan. In addition, issuers may offer catastrophic-only coverage with lower AV for eligible individuals. Actuarial Value, or AV, is calculated as the percentage of total average costs for covered benefits that a plan will cover. For example, if a plan has an AV of 70 percent, on average, a consumer would be responsible for 30 percent of the costs of all covered benefits. The 30 percent could be reached through a combination of co-pays, co-insurance and deductibles.