Sequester poised to take effect as partisan standoff over substitute continues

An estimated $85 billion in across-the-board spending cuts for fiscal year 2013 are set to take effect by midnight March 1 as Democrats and Republicans remain unable to agree on a plan to delay or replace them and a meeting at the White House between President Obama and congressional leaders from both parties yielded no last-minute solutions.

Senate sinks dueling proposals

Legislative action on the sequester was confined to the Senate, where a proposal from Majority Leader Harry Reid, D-Nev., that would delay the spending cuts until next year and offset the cost with a mix of tax increases and targeted spending cuts failed on procedural grounds February 28, as did a rival GOP proposal that would have allowed President Obama to replace the sequester cuts with $85 billion in spending cuts of his choosing, subject to certain restrictions.

Democratic proposal – A motion to move forward with Reid’s American Family Economic Protection Act (S. 388) was defeated by a vote of 51-49, short of the 60 votes required for passage. Reid’s proposal would delay the impending budget sequester until next year by replacing this year’s savings with $110 billion in offsets, split equally between tax and spending provisions.

Major tax offsets in the bill would:

- Impose a 30 percent “fair share” tax on taxpayers with adjusted gross income (AGI) over $1 million, ($500,000 for married taxpayers filing separately) – less a portion of charitable contributions deducted for the taxable year – if their “fair share” tax liability exceeds the sum of their regular tax liability, plus the alternative minimum tax, plus payroll tax for the taxable year, less certain credits. The “fair share” tax, a version of the president’s so-called “Buffett rule,” would be phased in pro-ratably for taxpayers with AGI between $1 million and $5 million (50 percent of these thresholds in the case of a married individual who files separately). These thresholds would be adjusted for inflation beginning in 2014. The tax would apply to taxable years beginning after December 31, 2013.

- Disallow deductions for expenses paid by a taxpayer to eliminate a trade or business (or any line of business or functional unit that is part of any trade or business) currently located inside the United States and move it outside the United States. Subpart F income attributable to a controlled foreign corporation also could not be reduced by any such expenses. Expenses subject to the deduction disallowance would be limited solely to those associated with the relocation of the trade or business, including amounts deductible under section 162, permit and license fees, lease brokerage fees, equipment costs, and other similar expenses identified in subsequent Treasury guidance. The deduction disallowance would not apply to ongoing operating expenses of the trade or business or to costs for severance pay or similar expenses. The proposal would be effective for expenses paid or incurred after the date of enactment.

The measure also includes a provision that would extend an existing per-barrel tax on oil production to oil produced from tar sands.

GOP proposal – The Senate also rejected by a vote of 38-62 a bill (S. 16) introduced by Republicans Pat Toomey of Pennsylvania and Jim Inhofe of Oklahoma that would require President Obama to submit to Congress a “qualifying sequester replacement plan” by no later than March 15, 2013. The replacement plan would have to permanently cancel roughly $85 billion in discretionary appropriations or direct spending so long as no more than $42 billion is canceled from defense spending.

Under the bill, the president’s replacement plan would receive expedited consideration in both chambers and could be rejected only if both chambers passed a joint resolution of disapproval.

No surprises here – The outcome of both votes was generally regarded as a forgone conclusion as neither bill was expected to advance in the Senate. Republicans had already declared the revenue discussion closed with the enactment of the American Taxpayer Relief Act on January 2 and have maintained since then that they would not accept a sequester substitute that included tax increases.
“[The president] already got hundreds of billions in new revenue earlier this year,” Senate Minority Leader Mitch McConnell, R-Ky., said on the Senate floor before the vote on the Democratic proposal. “Now it’s time for the balance part of the equation, and that means keeping our promise to reduce spending.”

Democrats likewise reiterated their insistence on a “balanced” replacement package as Reid took to the floor and called on Republicans to “give Congress true flexibility...to cut wasteful subsidies,...close unnecessary tax loopholes, and...ask the richest of the rich to contribute a little more.”

Boehner: We did our job

For their part, House Republican leaders have not introduced a sequester replacement package in the 113th Congress and have declared that they will not offer a proposal until the Senate clears a bill of its own.

The House approved two spending-cuts-only bills last year to replace the sequester; but those proposals were never taken up in the Senate and they expired when the 112th Congress ended. (House GOP leaders in recent weeks blocked a Democratic proposal from coming to the floor that would have offset a sequester delay by raising $120 billion through a mix of spending cuts and tax increase provisions.)

“Republicans in the House passed legislation almost a year ago in May, and again in December, to avert the president’s sequester and help put us on a path to a balanced budget,” Speaker John Boehner, R-Ohio, said in a February 28 news release following the unsuccessful votes in the Senate. “Now that today’s political stunt to raise taxes has failed, it’s time for the president and Senate Democrats to do the hard work that is necessary to pass a bill in the Senate so we can begin to resolve this issue.”

White House meeting

An hour-long White House summit between the president and Democratic and Republican congressional leaders on March 1 apparently did not mend the partisan rift. Boehner told reporters as he left the White House that the “discussion about revenue, in my view, is over. It’s about taking on the spending problem here in Washington.”

In press briefing after the meeting, President Obama blamed the failure to avert the sequester on “a choice that Republicans in Congress have made” to reject proposals to close tax “loopholes” that benefit corporations and more affluent individuals.

The president stated that there is a silent bipartisan “caucus of common sense on Capitol Hill” that is willing to accept a combination of entitlement reforms, targeted spending cuts, and revenue increases as part of a deal to turn off the sequester, and that he will continue to reach out to these lawmakers over the next several weeks.

Next steps

With the sequester now a certainty, the question becomes how long the mandatory cuts will be allowed to remain in effect – that is, how long it will be before one side or the other in the tax-versus-spending debate accepts proposals it had previously rejected in order to delay or turn off the spending cuts.

Lawmakers could attempt to ameliorate – if not resolve – the sequester later this month when they take up a new continuing resolution (CR) to fund government operations for the rest of fiscal year 2013. (The current CR expires March 27.) The House is expected to put a bill on the floor the week of March 3 that would extend government funding at sequestration levels for the next six months but give certain agencies – primarily those related to defense, military construction, and veterans’ programs – greater flexibility in administering their appropriations. However, Senate Democrats have been cool to the idea of offering protections to defense programs while providing none to other domestic programs.

Both chambers have another built-in opportunity to address the sequester as part of the fiscal 2014 budgeting process that will play out this spring. The House and Senate have already confirmed that they will clear their respective tax and spending blueprints by the statutory deadline of April 15. Senate Budget Committee Chair Patty Murray, D-Wash., has said that her budget will call for increased revenue from closing certain tax provisions benefitting corporations and high-income individuals. House Republicans have not yet revealed specific details of their upcoming budget resolution, except to say that the plan will produce a balanced budget by fiscal year 2023 without calling for tax increases.
The White House, which missed its February deadline for sending its budget package to Congress, has promised to release a proposal this month, but has not announced a specific date.

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