

Tax Policy Update

March 5, 2018

NUMBER OF THE WEEK: \$50,000



Photo: Getty Images/Ralf Hirschberger/DPA

The potential tax hit for those who grabbed a swag bag at the Oscars on Sunday. The IRS considers these fancy giveaways as income and can collect taxes based on the value of the gifts, which is estimated to be somewhere around \$100,000. The [gift bag](#) includes luxury vacation packages, cosmetics, clothes, and high-tech gadgets.

LEGISLATIVE LANDSCAPE

Rough Riders? Congressional appropriators are trying to finish writing the FY 2018 omnibus spending bill this week. Some sections, like transportation and commerce, are done, while others are still baking. Lawmakers are hoping to introduce the legislation early next week, which will give them several days to debate and pass the package before the March 23 government-funding deadline. But don't be surprised if Congress ends up cutting it close.

The FY 2018 omnibus would fund the federal government through the remainder of the fiscal year. As with almost all must-pass legislation, the omnibus will likely include unrelated policy riders, such as a fix for Sec. 199A.

Sec. 199A provides a deduction that incents farmers to sell their crops to agricultural co-ops rather than other companies. Non-cooperatives have argued that the deduction places them at a competitive disadvantage. The *Tax Policy Update* team expects the fix (which will be retroactive) to make it into the omnibus.

Lawmakers are also talking about adding provisions to address telecom, healthcare (i.e. the Alexander-Murray market stabilization bill), and the online sales tax. Democrats are already warning Republicans against sneaking in any poison-pill riders, which could jeopardize the bill's passage. That said, a shutdown is unlikely as congressional leaders are determined to get the omnibus done as soon as possible.

Hatch Gives IRS Some Love. Senate Finance Chairman Orrin Hatch (R-UT) is open to increasing funding for the IRS, acknowledging that the tax-collection agency has been doing its best despite the political challenges in the past few years. "I want to help them down there. I think they do a very, very good job, much better than people give them credit for," Hatch said at a tax event hosted by the American Enterprise Institute last week.

Treasury Secretary Steven Mnuchin has previously asked Congress for an additional \$400 million, so that the agency has adequate resources to implement the new tax law. Back in February, the White House unsuccessfully asked lawmakers to provide an extra \$90 million for the IRS in the bipartisan budget agreement. It remains to be seen whether the beleaguered agency will see a meaningful funding boost in the forthcoming omnibus bill.

Crapo's Banking Bill Hits the Floor. The Senate will take up consideration of S. 2155, the [*Economic Growth, Regulatory Relief, and Consumer Protection Act*](#) — a bill that would ease regulatory burdens for small financial institutions such as credit unions, community banks, and regional banks. The bipartisan measure also aims to improve access to mortgage credit and consumer protections for veterans and victims of fraud. Of note, the bill would exempt banks with less than \$250 billion in assets from the Fed's enhanced prudential standards. Under current law, banks with more than \$50 billion are subject to higher capital requirements and annual stress tests.

Senate Banking Chairman Mike Crapo (R-ID) is planning to drop a few additional provisions into the bill via a manager's amendment on the floor. These provisions are expected to include a handful of minor bills that have already cleared the House — such as those dealing with capital formation. Crapo has been meeting with House Financial Services Chairman Jeb Hensarling (R-TX) to "pre-conference" the bill, which will allow the House to quickly pass S. 2155 when it gets the bill from the upper chamber.

Barring any last-minute controversial additions, passage is expected by the end of the week — despite strong opposition from progressives such as Sens. Elizabeth Warren (D-MA) and Sherrod Brown (D-OH).

REGULATORY WORLD

Carried (Interest), Things They Change My Friend. The Treasury Department and the IRS issued guidance ([Notice 2018-18](#)) announcing their plans to issue regulations clarifying that S corporations are subject to the three-year holding period for carried interest under the GOP tax law. The clarification seeks to prevent managers of hedge funds from creating shell companies (S corporations) to avoid the three-year holding period.

Whether the Treasury Department has the authority to impose that interpretation of the statute is an open question. In a press release announcing the guidance, Treasury Secretary Steven Mnuchin said that the Treasury and the IRS will implement the tax law “as Congress intended.”

TIGTA Report on IRS Employee Misconduct. Earlier this month, House Ways and Means Committee Chairman Kevin Brady (R-TX) and Senate Finance Committee Chairman Orrin Hatch called on IRS Acting Commissioner David Kautter to immediately implement screening procedures to ensure that employees with serious conduct issues are not receiving bonuses.

The letter comes after a Feb. 13 Treasury Inspector General for Tax Administration (TIGTA) [report](#) that found over the last two fiscal years, the agency spent about \$1.8 million in awards to 1,962 employees who had been subject to disciplinary actions.

Similarly, a 2014 TIGTA report found that between Oct. 1, 2010, and Dec. 31, 2012, more than 2,800 IRS employees with recent substantiated conduct issues received \$2.8 million in monetary awards. TIGTA recommends that the IRS assess the feasibility of implementing a policy requiring the agency to consider conduct issues, including tax compliance status, prior to issuing awards.

TIGTA Report on Incorrect Refunds. TIGTA released a report titled, [“Employer Noncompliance with Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims before Refunds are Paid.”](#) The watchdog agency noted that the IRS issued \$8.2 billion worth of refunds for more than 1.4 million tax returns with wage discrepancies. The refunds were sent even though the wage information reported on the returns did not match wage information reported on third-party W-2 forms from employers.

The \$8.2 billion in refunds included \$4.3 billion in the Earned Income Tax Credit (EITC) and \$1.7 billion in the Additional Child Tax Credit (ACTC). For about 661,000 of these returns, the IRS received no third-party W-2 forms prior to the refunds being released. These returns had refunds totaling almost \$3.7 billion. Missing or late W-2s hinder the IRS' verification capabilities, according to the report.

TIGTA's findings were based on an audit of 8.4 million electronically filed tax returns as of Feb. 15 of last year with either EITC or ACTC claims, or both. The IRS identified 1.5 million returns with discrepancies, of which it flagged 70,406 for further fraud or examination review. In 2016 alone, the IRS has estimated that it improperly issued \$16.8 billion in EITC payments.

LINE ITEMS

1. The White House announced the nomination of Michael J. Desmond to be the chief counsel at the IRS. Desmond served as the tax legislative counsel at the Department of the Treasury from 2005-2008.
2. The House passed, 245-169, [H.R 4296](#) – a bill that would allow banks to calculate operating risk by using forward-looking models that reflect each bank’s business activities.
3. Senate Appropriations Chairman Thad Cochran (R-MS) announced that he will be leaving Congress on April 1 due to health issues.
4. This week, the House will take up consideration of H.R. 4607, the [Comprehensive Regulatory Review Act](#), which would expand the required comprehensive review of financial regulatory requirements. The review must be completed by the Federal Financial Institutions Examination Council, CFPB, NCUA, OCC, FDIC, and Federal Reserve Board. The review must be conducted every 7 years and regulators must consider tailoring regulations to limit specified burdens.

COMMANDER-IN-TWEET



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4:10 PM - 4 Mar 2018

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22K 25K 110K

IN THE QUEUE

Congressional Activity

Tuesday, 3/6

House Appropriations Committee

Subcommittee hearing on the Treasury Department's FY 2019 budget request. Secretary Mnuchin to testify.

House Appropriations Committee

Subcommittee hearing on the Labor Department's FY 2019 budget request. Secretary Acosta to testify.

Senate Finance Committee

Full committee hearing on "Protecting E-commerce Consumers from Counterfeits."

House Financial Services Committee

Markup of FY 2019 budget views and estimates.

House Transportation Committee

Hearing to examine the administration's infrastructure proposal.

Wednesday, 3/7

House Transportation Committee

Subcommittee hearing on "Building a 21st Century Infrastructure for America: Long-Term Funding for Highways and Transit Programs."

House Appropriations Committee

Subcommittee hearing on the CFTC's FY 2019 budget request with Chairman Chris Giancarlo testifying.

Joint Economic Committee

Hearing on "The Economic Report of the President" with Council of Economic Advisers Chairman Kevin Hassett testifying.

House Financial Services Committee

Subcommittee meeting to discuss H.R. 5059, the *State Insurance Regulation Preservation Act*.

House Financial Services Committee

Subcommittee hearing on "Legislative Proposals to Reform the Current Data Security and Breach Notification Regulatory Regime."

Agency Activity

Thursday, 3/8

SEC

Investor Advisory Committee holds its quarterly meeting.

Other Activity

Tuesday, 3/6

Institute of International Bankers

IIB holds its Annual Washington Conference, bringing together senior U.S. and international government officials and industry leaders to address key policy issues.

Roll Call

“Health Care Decoded” event where participants and experts will discuss key questions that health care industry stakeholders and policymakers will face in 2018.

Wednesday, 3/7

The Economic Club of Washington

Discussion with the Israeli Prime Minister Benjamin Netanyahu.

Thursday, 3/8

Blockchain in Energy Forum 2018

Join GTM Research to learn the basics of blockchain and other distributed ledger technology.

Politico

Event on the “The Future of Prosperity” to examine the rising cost of college and retirement with special guest Mark Calabria, chief economist with the Office of the Vice President.

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