Solomon said that from a policy perspective, the transferor-by-transferor approach yields the right answer, but Laurie Matthews, senior legislation counsel to the Joint Committee on Taxation, agreed that the parenthetical language is confusing.

Double Benefits

There was speculation over whether double use of basis was appropriate to limit gain recognition in the reorganization context under sections 355 and 368(a)(1)(D). The new rule, in conjunction with the liability assumption rule, could operate to allow asset value to be pulled out of a subsidiary twice, panelists acknowledged.

The double benefit scenario prompted Solomon to ask Matthews about the effective date of technical corrections.

Technical corrections are generally effective as of the date of the original legislation, Matthews responded.

> ***Alexander added that there are Supreme Court cases that say taxpayers should be suspicious of an interpretation of the code that would allow a cost to be recovered twice.***

Alexander added that there are Supreme Court cases — *Ilfeld* and *Skelly Oil* — that say taxpayers should be suspicious of an interpretation of the code that would allow a cost to be recovered twice. It is not clear that Congress intended any double benefit here, he said.

Another aspect ripe for a technical correction is the application of section 334(b)(1), which would cause assets subject to U.S. tax to be marked to market in an upstream liquidation under section 332, according to Eisenberg.

Solomon said Eisenberg's point was valid.

Congressional staffs continue to receive comments on needed technical corrections, said Matthews. Sometime there may be another bill with technical corrections in it, she said, and she encouraged practitioners who spot additional problems to let staff members know about them. ■

Budget Panelists Say Reforms Can Come Only Through Compromise

By Wesley Elmore — welmore@tax.org

Bipartisanship was the theme last week as panelists at a conference sponsored by the Committee for a Responsible Federal Budget (CRFB) said Republicans and Democrats must work together if they expect to make any progress on tax reform, budget deficits, and Social Security reform.

Speakers pointed to past successful reform efforts — such as the Social Security reform actions of 1983, the Tax Reform Act of 1986, and the discretionary spending caps and ''pay as you go'' budgetary rules used in the 1990s — as evidence that bipartisan progress can be made on the major agenda items of the 109th Congress. Several speakers also argued that tax, Social Security, and budget issues are all linked and should not be looked at in a vacuum.

Bill Hoagland, budget adviser to Senate Majority Leader Bill Frist, R-Tenn., said President Bush has tried to keep the issues separate for ''tactical'' reasons, but action on all of them comes down to whether Congress can ''walk and chew gum at the same time.''

Fundamental Tax Reform?

Bill Frenzel, former member of the House Ways and Means Committee and current member of the president's tax reform panel, moderated the panel on tax reform and heard several suggestions from panelists for ideal systems of taxation.

But Brookings Institution fellow William G. Gale, who testified last week before the tax reform panel at its first meeting, said it's easy for people to come up with ideal tax systems on paper that could ''never exist in the real world.'' Paraphrasing Defense Secretary Donald Rumsfeld, Gale said that when looking at tax reform options, ''we need to start with the political system we have and not the one we would like to have.'' (For coverage of the tax reform panel meeting, see p. 879.)

> ***Paraphrasing Defense Secretary Donald Rumsfeld, Gale said that when looking at tax reform options, 'we need to start with the political system we have and not the one we would like to have.'***

Gale predicted that when the panel offers its reform proposals, options will not consist of ''fundamental reform,'' but will instead follow the lead of the 2001 and 2003 tax cuts by cutting off the income tax "one limb at a time" to eventually result in a flat tax. That would lead to the worst of both systems, resulting in a regressive tax system and the creation of "enormous" tax shelters, he said.

Kevin Hassett of the American Enterprise Institute (AEI), however, wasn't shy about recommending more fundamental reform options, citing different versions of a consumption tax or an income tax "without all the junk in it" as options that would raise the country's gross domestic product while making both high-income and low-income individuals better off.

Hassett told Frenzel that his panel should look past the political fallout that might come from eliminating incentives like the child credit and the mortgage interest deduction and instead work to reform the tax system for "the public good."

"If we don't have politicians who are willing to do that, we should just stop tax reform right now. We shouldn't even study it," Hassett said.

Norm Ornstein, also with AEI, said he too hopes the panel members will "broaden their horizons" because as the current system continues to "whack away" at income and corporate taxes, the government will have to rely more and more on payroll taxes.

One major reform that Gale, Hassett, and Ornstein all agreed was worth studying is the introduction of a value added tax.

Leon Panetta, former congressman and chief of staff for President Bill Clinton, said that ultimately, for any reform effort to work, the president would have to work with Democrats on a compromise because he will not be able to "slam dunk" the issue.

> ***One major reform that Gale, Hassett, and Ornstein all agreed was worth studying is the introduction of a value added tax.***

Gale, however, stressed that lawmakers should look at "two major tax issues coming to a head" before looking too hard at overall reform: the expiring tax cuts and the alternative minimum tax.

The tax cuts are a "first-order economic issue" that should not get lost in the "hype and hyperbole" of tax reform, Gale said. The costs of the cuts would have to be paid for through other tax increases or "spending cuts that are far off the political spectrum," he said.

Spending Cuts or Tax Increases?

Spending cuts that appeared in the White House's recent budget proposal were a focus of the conference's budget panel, with Jim Horney of the Center on Budget and Policy Priorities saying the cuts in domestic spending were "more than offset" by new tax incentives and increases in defense spending included in the budget — proving, he said, that tax cuts are more important to the Bush administration than controlling the nation's deficits.

To reduce deficits, lawmakers must use a combination of spending cuts and revenue increases, Horney said.

But that appears easier said than done. Hoagland said controlling spending — not raising taxes — is the answer to reducing deficits. Maintaining the level of spending cuts that the president advocates over the next five years will be tough, but necessary, he said.

"It's easy to find fault with the president's budget," Hoagland said. "It's not so easy to find an alternative."

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Panelists agreed that any alternative should be bipartisan. Horney said he believed many Democrats would jump at the chance to sit down with the president and work out a bipartisan budget solution, but Hoagland appeared doubtful that would happen.

For a bipartisan solution to come about, members of both parties should be willing to provide cover for one another when cutting spending and increasing taxes, Horney said. Panetta agreed, saying everyone should be "willing to walk the plank together."

CRFB President Maya MacGuineas said that in recent years, as it has become more difficult for Congress to come to a consensus on the annual budget, lawmakers instead budget "pretty much entirely through the tax code," which "makes taxes far less efficient and far less transparent."

But What About Social Security?

Ornstein pointed to Social Security reform as a harbinger of things to come on other issues, such as the budget and particularly tax reform. If discussions on Social Security continue to break down along partisan lines, he said, that will "reverberate" into other areas and could prevent other items on the Bush agenda from getting done.

Government Accountability Office Comptroller General David Walker said the Social Security debate has gotten "too partisan," preventing real action from taking place as officials debate the size of the problem.

"It clearly would be prudent to act sooner rather than later," Walker said.

Gene Sperling of the Center for American Progress, who served as Clinton's national economic adviser, said the debate so far has been "the dumbest discussion ever." He added, "It's better to act early if you act responsibly."

While other panelists agreed that the debate did not get off to a good start, several said Congress is capable of acting on Social Security reform this year, but only if members remain flexible and are willing to work together. (For related coverage, see p. 889.)■

Observers Urge Congress to Reject Proposed E-Filing Extension

By Warren Rojas — wrojas@tax.org

Although they embraced most of the tax administration proposals in President Bush's fiscal 2006 budget blueprint, several commentors criticized a plan to postpone the April 15 filing deadline to pad the Service's e-filing figures.

The revenue-neutral reform bundle — which appears to have been derived largely from the House-passed Taxpayer Protection and IRS Accountability Act of 2003 (H.R. 1528) and the Senate-passed Tax Administration Good Government Act (introduced as S. 882 and later folded into H.R. 1528) — features several repeats from the administration's fiscal 2005 budget, including:

- Amending section 1203 of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA '98; P.L. 105-206): The plan would drop late-filed returns and employee vs. employee flare-ups from the so-called 10 deadly sins list and add unauthorized access violations to the roster of offenses. The IRS would also be required to flesh out punitive guidelines for various offenses while retaining immediate dismissal power.
- Strengthening frivolous filing penalties: The frivolous return penalty would jump from $500 to $5,000, and the IRS would reserve the right to void any due process requests, offer in compromise deals, or installment agreements based on frivolous returns. Frivolous filers would also be tagged by the IRS computers — Treasury suggests creating an unspecified administrative record — until a "reasonable period of time" passes since the questionable filing.
- Scrapping installment agreements with negligent taxpayers: This provision would allow the IRS to pull the plug on installment deals with late tax return filers.
- Streamlining judicial review of collection due process cases: This proposal makes the U.S. Tax Court the "exclusive venue" for all CDP appeals.
- Stripping the counsel review guidelines for offers in compromise: This step absolves the chief counsel from having to file an opinion in most OIC cases (including those above $50,000) and instructs Treasury to draft more detailed OIC opinion guidelines.