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Capitol Account:

A Memo to AICPA Key Persons

Washington, D.C

August 2001

AICPA Scores Two Home Runs with Tax Cut Bill

Institute's GST and Retirement Planning Provisions Included

The AICPA scored two home runs when President Bush signed his \$1.35 trillion tax cut bill into law.

First, the new law includes the AICPA's package of generation-skipping transfer tax (GST) provisions. The provisions will provide statutory authority for the IRS to grant regulatory relief for late allocations of the GST tax exemption, so taxpayers will not necessarily have to face unintended or punitive taxes. The AICPA proposal also makes other technical changes to the GST tax rules that will substantially alleviate their traps for unwary taxpayers. The Institute fought hard to have its GST proposal included because it will be 2010 before the new law fully repeals the estate and GST taxes (if indeed, that actually occurs) and taxpayers need help now in avoiding these traps.

Second, the AICPA successfully urged Congress to include its retirement education proposal in the tax bill so that employers can provide retirement advice to their employees on a tax-free basis; that is, the cost of the advice is deductible to the employer, but is not included in employee income. The new provision, effective next year, does not apply to tax return preparation, will drafting, or similar services, but it will allow all employers with qualified retirement plans to provide retirement planning assistance to their employees without concern that the cost of that advice is taxable to the employee.

Another change made by the new law that the Institute has long supported is marriage penalty relief. While the marriage penalty relief provisions of the new law are not as broad-based as the AICPA would have preferred, some relief begins to phase in starting in 2005.

One provision the AICPA supported that was dropped out of the bill was an acceleration of the health insurance deduction for self-employed individuals. Therefore, the 100% deduction will not be available until 2003.

While all the provisions of the new law expire in 2011, unless a future Congress and President act to extend them, Members of Congress are already laying plans to make the changes permanent.

cc: Board of Directors
Members of Council

**Fiscal Year Flexibility—
Back to the Drawing Board**

Cost continues to stand between us and fiscal year flexibility for small businesses. The budget surplus seemed to provide a political opportunity earlier this year to amend the calendar-year requirements imposed on small businesses by the Tax Reform Act of 1986, but the private revenue estimates on our most recent legislative proposal were unacceptably high. The unexpectedly high revenue loss arises, in large measure, because the dramatic growth in the number of passthrough entities (partnerships, S corporations, LLCs, etc.) over the past several years results in many billion dollars of income that would be potentially subject to tax deferral should the owners of those businesses elect to use a fiscal, rather than a calendar, year end.

The Tax Division task force working on the issue is now trying to refine the proposal to bring foregone revenues within an acceptable range.

AICPA Seeking Exemption for CPAs from Privacy Notification Regs

The AICPA has been meeting with the Federal Trade Commission (FTC) since January in order to obtain an exemption for CPAs to the privacy disclosure requirements of the Gramm-Leach-Bliley Act. The FTC is receptive to our arguments that CPAs should be exempt, but may not be able to make the change without modifying the present regulation. We are hopeful that a proposed new regulation will be forthcoming. (For information about how to comply with the FTC privacy requirements, see the AICPA's practice guide at <http://ftp.aicpa.org/public/download/news/ftc.doc>.)

Offsets Part of Equation for Business Tax Breaks

The shrinking budget surplus has lawmakers scrambling for tax offsets in order to deliver tax cuts to the business community. Congressional Republicans' goal is to add small business tax breaks to the bill to increase the minimum wage, in order to reduce its sting on small business. However, Senate Majority Leader Tom Daschle (D-SD) says he wants future tax cut bills to include offsets to pay for the cost of those tax breaks. Meanwhile, Administration spokespersons say the White House won't push for business tax cuts until 2002.

Business Tax Shelter Issue Rumbles Back to Life

The business tax shelter issue has rumbled back to life in Congress this summer.

In the House, Rep. Lloyd Doggett (D-TX) reintroduced a modified version of his bill from last Congress that the accounting profession opposed. Because the bill (H.R. 2520) would generate revenue for the government, opponents of the compromise patients' rights bill (H.R. 2563) developed by President Bush and Rep. Charlie Norwood (R-GA-10th) grabbed it as an amendment to help pay for the costs of the Democratic alternative to the HMO reform bill that the House passed on August 2nd. This attempt failed. The AICPA believes that the Doggett bill remains so broad and vague it threatens many normal business transactions.

In the Senate, Finance Committee Chairman Max Baucus (D-MT) and Ranking Minority Member Charles Grassley (R-IA) released a draft bill to require greater disclosure of potentially abusive tax shelters. The draft bill would not establish any new penalties on illegal transactions, but it would increase existing penalties. The draft bill is the third in a series of bills

released by the Finance Committee. The first two were released last Congress.

The AICPA will submit comments to the Finance Committee on the draft bill and has already determined that it contains some of the same weaknesses we identified in the first two draft bills.

Joint Tax Committee Simplification Study Triggers Hearings; AICPA Set to Testify

The tax simplification study released this spring by the Joint Committee on Taxation has elevated Congressional awareness of the monstrous complexity in the tax code and triggered a series of joint hearings by the House Ways and Means Subcommittees on Oversight and Select Revenue Measures. The AICPA anticipates testifying this fall at one of the next hearings in the series.

The AICPA historically has been the most outspoken champion for tax simplification, hammering the point home at numerous Congressional hearings. The Joint Committee's report identifies some of the same culprits of complexity as we have—for example, the phase-ins and phase-outs that pervade the system and the alternative minimum tax. Our testimony will outline where we agree with the recommendations of the Joint Committee's study and where we think it did not go far enough.

Collaborative Effort with TEI and ABA Tax Section Focuses on Joint Tax Study

Our continuing collaborative effort with the Tax Executives Institute and the American Bar Association Section of Taxation to encourage Congress to simplify the tax code currently is focused on the Joint Tax Committee's tax simplification study.

We have scheduled a December conference on Capitol Hill that will serve as a forum to gather detailed comments on the Joint Tax Committee's study. The invitation-only conference will bring together lawmakers and their staffs, Treasury and IRS officials, tax experts in academe, and leaders of professional organizations. Joint Tax Committee staff will participate and are looking forward to the conference to help propel the tax simplification discussion and launch meaningful tax simplification legislation.

Deadline Looming for Congressional Action on Internet Tax Moratorium

Congress needs to sprint if it's going to act on Internet taxation before the current three-year moratorium expires on October 21, 2001. The House is positioned for a quick start this fall, but in the Senate, where jurisdiction over Internet taxation is split between the Finance and Commerce Committees, efforts to reach a bipartisan compromise are stalled.

The House Judiciary Commercial Law Subcommittee passed a bill on August 2, 2001, to maintain and expand limits for five years on the taxation of Internet service and commerce. The full Judiciary Committee is expected to approve the bill (H.R. 1551) in September and then send it to the full House for a vote.

The bill's sponsor, Rep. Christopher Cox (R-CA) and other supporters, would like to attach it to one of the appropriations bills to help ensure its passage by the Senate. However, before H.R. 1551 gets to the Senate, House supporters will have to defeat an amendment that Rep. Ernest Istook (R-OK) plans to

offer. His bill (H.R. 1410) would extend the current moratorium for four years, but it would also include language encouraging states to form a compact to collect sales taxes on electronic commerce. The National Governors' Association supports the Istook bill and opposes the Cox bill. It doesn't take a crystal ball to see that the "inside the beltway" prediction on this issue is that Congress will act at the eleventh hour after cobbling together a compromise which is likely to extend the deadline and that will be rolled into an appropriations bill.

House Commerce Committee Begins to Write Internet Privacy Bill

An Internet privacy bill is being drafted by members of the House Commerce Committee that Chairman Billy Tauzin (R-LA) plans to circulate for comment after Congress returns from its August break. Tauzin said he intends to kick off serious negotiations for the electronic privacy data bill this fall.

Tauzin announced his decision to proceed with legislation at a Capitol Hill news conference on June 27, even though there is disagreement about whether federal legislation is required.

His decision comes after a series of online privacy hearings held by the Committee's Subcommittee on Trade, which is chaired by Rep. Cliff Stearns (R-FL). Many of the witnesses have argued at the hearings that privacy legislation now would be premature. However, Chairman Tauzin expressed concern at the news conference that self-regulation may not adequately protect all consumers from individuals who are not "good players," while also acknowledging the "need to move very carefully" on privacy.

Subcommittee Chairman Stearns also noted that drafters of the bill have to take into account the individual state privacy laws and the European Union (EU). Stearns said the EU's privacy rules are too restrictive and predicted that because only 40 U.S. companies have agreed to the EU's safe-harbor provisions there's trouble ahead for the EU. The EU just began enforcing its privacy pact on July 1.

The Commerce Committee's draft privacy bill is expected to provide a safe harbor for Internet sites that follow voluntary privacy standards and to establish baseline standards that all other sites would have to meet. Tauzin said opt-out provisions will be the core model for the bill and he expects the bill to preempt state laws in order to ensure minimum national privacy requirements.

Privacy Commission Bill Approved by House Subcommittee

On another front in the privacy arena, the House Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations approved a bill to establish a commission to study privacy issues and report to Congress.

The bill, H.R. 583, sponsored by Rep. Asa Hutchinson (R-AR), includes the provision sought by the AICPA to require that the commission's report include a look at third-party verification as an enforcement mechanism. Third-party verification means that an objective third party examines a business's privacy policy to make sure that the privacy representations are true and that the business is following them in day-to-day transactions. (WebTrust

Version 3.0, and its related WebTrust Program for Online Privacy, is an example of a third-party verification program currently available in the private sector.) Third-party verification of privacy policies could involve responsibilities for the profession with related liability risks.

The outlook for H.R. 583 is uncertain, particularly in light of Chairman Tauzin's decision to write privacy legislation. Democrats and consumer advocates have long opposed establishment of a privacy commission, instead advocating that Congress immediately begin debate on legislation to protect consumers' privacy when using the Internet.

Senate Approves Pitt to Chair SEC

The Senate unanimously confirmed Harvey Pitt to chair the U.S. Securities and Exchange Commission (SEC) on August 1, 2001. During his confirmation hearing before the Senate Banking Committee, Pitt pledged a review of SEC rules and endorsed the current process of having financial reporting standards set in the private sector and FASB's role in that process.

Following the White House's announcement in May that the post would go to Pitt, Barry Melancon, President and CEO of the AICPA, said President Bush has "nominated a very experienced individual to be the new SEC Chairman who has the background, intellect, and capacity to challenge the status quo." Melancon noted that today's financial world "has changed dramatically" since the current securities laws were created in 1933 and 1934 and that Congress needs to review the laws to see where they need to be modernized in order to make sure our statutory structure meets today's fast paced global requirements. "Harvey Pitt," Melancon said, "is very knowledgeable about the many issues and opportunities facing the SEC and the markets. We are very confident we can create an open and progressive dialogue with the Commission for the benefit of the public under his leadership. We have every confidence in Pitt's ability to lead the SEC at a critical time in its history."

Pitt, a Washington securities lawyer formerly with Fried, Frank, Harris, Shriver & Jacobson, was formally nominated to be the chairman of the SEC on July 10. Pitt served as the SEC's general counsel from 1975 to 1978.

The White House has not dropped any hints about whom it will nominate to fill the other two vacancies on the Commission. Prior to Pitt's confirmation only two of the Commission's five seats were filled. The terms of both the other Commissioners—Laura Unger and Isaac Hunt—have expired, but they are eligible to be reappointed. Commissioner Paul Carey died in June. The seat previously held by Commissioner Norman S. Johnson has been vacant since he left the SEC in May 2000.

Bush Social Security Commission Releases Interim Report

The draft report released by the President's Commission to Strengthen Social Security ignited this year's political debate about privatization of the Social Security system. The report outlines the challenges facing the program and makes the case for wholesale overhaul of the system, but does not recommend specific reforms. The Commission will recommend actual fixes in its final report, which will be released this fall.

The report has drawn a negative reaction from most Democrats who have

charged that it is alarmist. President Bush has a core of Republican supporters in Congress who favor establishing private Social Security accounts, but other Republicans are reluctant to take up such a hot issue when facing the mid-term elections in 2002.

The interim report, which was released in late July, is on the Commission's web site at <http://www.CommToStrengthenSocSec.gov>.

AICPA Supports Uniform International Accounting Standards at House Hearing

Tells Congress Current Financial Reporting Model Also Should Be Modernized

The AICPA told members of the House Subcommittee on Capital Markets that uniform international accounting standards will encourage the global flow of capital, but that standard setters, regulators, and the accounting profession should carefully consider the need to modernize the financial reporting system as well.

In his testimony, Robert K. Elliott, Immediate Past Chairman of the AICPA, said:

“Globally compatible financial presentations will make it easier for investors to compare companies and for companies to file in different markets. International accounting standards are critically important, but are not enough. We must also allow for a frequency and richness of disclosure that is closely aligned with the pace and nature of change in corporate prospects in our information age.

“Investors around the world need information that allows them to make good decisions. Capital flows are based on decisions by investors, and capital flows do not serve economic growth unless they represent economically useful decisions.

“The current financial reporting process—in the U.S. and overseas—is very much based on the assumption that profitability and growth depend on the physical assets needed to produce tangible products. This is the financial reporting model of the industrial age.

“We are no longer in an industrial age. We still have elements of it in our economy, but value today is founded upon new technologies, globalization and intangibles such as brands, relationships, people, systems and knowledge. Reporting should not be limited only to financial information that looks back. Corporate prospects no longer vary just annually or quarterly, as capabilities for rapid disclosure are coming into being.”

The Subcommittee explored the importance of harmonizing international accounting standards in the first of a series of hearings planned by the Subcommittee to explore its new jurisdiction over accounting issues. The jurisdiction was shifted to the Subcommittee from the House Energy and Commerce Committee at the beginning of this year when GOP leaders reorganized committee jurisdictions.

A copy of the AICPA testimony is available at http://ftp.aicpa.org/public/download/news/elliott_6_7.pdf.