

From the Editor:

August Heat on Capitol Hill

By Jon Almeras — jalmeras@tax.org

It was hot in Washington last week. August rolled in with temperatures climbing into the mid-90s, and local governments issued “code orange” warnings about air quality. Perhaps it was the heat getting to them, but House members’ tempers were hitting code orange and higher over a procedural vote taken late Thursday night on an amendment to an agricultural funding bill. After a shouting match broke out on the House floor, GOP members walked out in protest, believing the Democrats had gaveled the procedural motion closed to rig the outcome before voting was over.

On Friday morning, *The Hill* reported that Minority Leader John Boehner was trying to soothe his caucus, and Majority Leader Steny Hoyer was on the House floor trying to smooth things over as well. With the August recess about to begin, maybe it’s time everyone headed to the beach to cool off, literally and figuratively.

In Limbo

The dust-up left some House bills in limbo, including an energy package that includes \$15 billion in tax cuts. At press time, the House was scheduled to take up the bill August 4. The package would give tax breaks to renewable and alternative sources of energy while scaling back tax breaks for oil companies. Republicans have criticized the bill, citing the importance of coal and oil to the economy, and the White House has issued a veto threat because the bill would raise taxes (p. 442).

Speaking of things being in limbo, the nomination of Jim Nussle to head the Office of Management and Budget has been held up. The nomination made it through two committee votes last week, but two senators have placed holds on it. Bernard Sanders is one of the holding senators, but the other remains anonymous. The holds mean that a floor vote likely won’t happen until after Labor Day (p. 443).

A few things did get done in Congress last week. First both chambers passed an ethics reform package that includes earmark disclosure requirements. The White House has not signaled whether President Bush will sign the legislation, but it passed

both chambers with enough votes to override a veto (p. 445). The House and Senate have each passed their versions of the reauthorization of the State Children’s Health Insurance Program and an increase in the federal tobacco tax. The White House has threatened to veto both versions, so stay tuned (p. 447).

Kleinbard’s in at the JCT

The Hill’s top taxwriters, Max Baucus and Charles Rangel, last week announced that Edward Kleinbard of Cleary Gottlieb Steen & Hamilton, New York, is their choice for chief of staff of the Joint Committee on Taxation (p. 444). Kleinbard is known in policy circles for his interest in corporate tax reform, and he has written several articles for *Tax Notes* over the last few years advancing his proposal for a business enterprise income tax (see *Tax Notes*, Feb. 5, 2007, p. 547, and *Tax Notes*, Jan. 3, 2005, p. 97). In a letter to the editor, Matt Lykken of Baxter International commends Kleinbard for his interest in corporate tax reform and offers some advice for the new chief of staff about what reform needs to accomplish (p. 513).

Kleinbard spoke last week on behalf of the Securities Industry and Financial Markets Association at an IRS hearing on proposed foreign tax credit generator regs. Kleinbard and other speakers criticized the regs’ retroactive effective date and the characterization of some foreign tax payments as voluntary. Peter Faber of McDermott, Will & Emery questioned whether Treasury and the IRS have the authority to issue the regs. “If a statute does not work right, Treasury’s recourse is to go to Congress, not to try to twist it out of shape,” Faber said (p. 456).

The New York State Bar Association Tax Section met in Vermont recently, and members aired complaints to Treasury and IRS officials about recent regulations. Lee Sheppard gives the details on p. 452.

Carried Interests

The Senate Finance Committee held a hearing on carried interests last week featuring several witnesses representing the private equity industry. Many of the industry representatives who appeared at the hearing don’t support changing the treatment of carried interests, although one venture capitalist who appeared supports taxing carried interests at ordinary income rates (p. 439). As part of the testimony before Finance, the Private Equity Council circulated to members of Congress a paper by

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Prof. David Weisbach on why the arguments underlying carried interest legislation are “misplaced.” His paper appears on p. 505.

Finance also got something it's been asking for: a follow-up to last year's tax gap report from Treasury and the IRS. The 100-page report doesn't break any new ground on compliance, but Finance Committee ranking minority member Chuck Grassley called it “a good beginning” (p. 451).

Last year Congress made changes to the innocent spouse relief rules, granting the Tax Court jurisdiction to hear stand-alone equitable relief cases. One of the people who was instrumental in getting the legislation passed was Karen Hawkins, a California lawyer who volunteers with a Tax Court pro bono program. She tells reporter Jeremiah Coder the story of her journey (p. 457).

Commentary

In a special report, John Magee and Gerald Goldman of McKee Nelson argue that several appellate courts are misreading Supreme Court precedent when reviewing the application of the economic substance doctrine to the facts of a case. The proper standard of review, they assert, is clear error, not plenary review (p. 481).

In a practice article, Robert Wood analyzes whether a plaintiff in a civil suit can obtain damages for additional taxes the defendant's conduct caused the plaintiff to pay. The answer, Wood says, is “it depends” (p. 475).

Gene Steuerle delivers the last installment of his trilogy on measuring the “charitability” of tax-exempt organizations (p. 489). And in *Of Corporate Interest*, Robert Willens reviews the tax treatment of excess distributions paid to shareholders when they redeem stock (p. 499).

In *Tax Facts*, Eric Toder and Julianna Koch find that fewer businesses are organizing as C corporations in favor of flow-through entities like partnerships, limited liability companies, and S corporations. Between 1994 and 2004, the percentage of all business organizations that were C corporations fell from 40 percent to 25 percent (p. 491).

Who Said Tax Was Dull?

Finally, if you've ever looked into the deductibility of legal fees, you've come across *Gilmore* and the “origin of the claim” doctrine. The Supreme Court opinion hints at the sensational divorce that led to the tax case, but that belies the salacious soap opera — complete with adultery, alcoholism, a weeping lawyer, prostitutes, and an institutionalized wife — that scandalized San Francisco in 1953. In a fascinating tax history article, Prof. Joel Newman recounts it all (p. 493). If you happen to get a copy of the trial transcript, let us know. It would make a long (it's over 3,000 pages) but great beach read. ■