Biden's Corporate Tax Proposals Threaten Major Compliance Costs

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President Biden's plan to raise nearly $2 trillion in revenue from corporate and international tax reforms over the next decade threatens to pose a whole new round of headaches for tax practitioners trying to comply.

Corporate tax advisers are already coming off three years of adjusting to a new international tax regime thanks to the Tax Cuts and Jobs Act, and they're leery of going through this process again so soon, especially without sufficient opportunity to explain to policymakers the practical implications of Biden's proposed tax changes, according to Watson McLeish of the Tax Executives Institute.

Speaking during a June 16 webinar hosted by Tax Analysts, McLeish cited a study by the National Taxpayers Union Foundation that estimated U.S. businesses devoted 3.4 billion staff hours to tax compliance in 2019, amounting to $178 billion in compliance costs. "There's a significant cost here that we're self-inflicting. To the extent the minimum tax [on corporate book income] or any of the administration's other proposals adds to that, I think it's important that we should proceed with caution," he said.

Felicia Wong, president and CEO of the Roosevelt Institute, countered, saying that raising corporate taxes and closing corporate and international tax avoidance opportunities would actually be good for the economy as a whole. The TCJA's tax cuts failed to spark increased investment or growth, which suggests that there's room to raise significant revenue from businesses and the wealthy, she said.

"I would argue these tax increases, raising rates and improving collections, are an investment in economic fundamentals. We can't afford not to do them," Wong said.

But McLeish emphasized that the practical compliance challenges posed by Biden's proposals could be dramatic. He recalled that one TEI member at a midsize U.S. company with only a single tier of controlled foreign corporations described how her company ultimately had to forgo claiming the foreign tax credit under the global intangible low-taxed income regime in 2018 and 2019 because there simply wasn't enough staffing and software resources to finish the computation.

With Biden proposing to apply those calculations on a country-by-country basis, "you're looking at an exponential increase in the number of forms that would need to be filed, and quite frankly, you're looking at hiring more staff," McLeish said.

"Perhaps those are some of the jobs contemplated by the American Jobs Plan," McLeish added.

Not Alone

The difficulties of managing a new corporate and international tax regime wouldn't end with taxpayers.

"Any challenge a taxpayer faces on the front end in getting numbers on a tax return and complying with the tax law will be shared by IRS on the back end on the enforcement side," said Michael Desmond of Gibson, Dunn & Crutcher LLP.

Already, the IRS is effectively administering and implementing three sets of tax regimes, according to Desmond, a former IRS chief counsel. Pre-TCJA rules are still in play in many IRS exam and enforcement contexts; the IRS is only just starting to ramp up enforcement of the TCJA's provisions; and the Coronavirus Aid, Relief, and Economic Security Act's modifications to many tax rules are also in play, he said, though he added that he appreciates Biden's willingness to dramatically increase funding for the IRS.

Book Study

Biden's proposed minimum tax on corporate book income drew particular attention for the potential complications it poses.

Desmond acknowledged that financial statement reporting is already referenced in some provisions of the code, most notably section 451(b), enacted by the TCJA, which references using financial statements to determine the timing of income inclusion. But that was "a very challenging guidance project when I was chief counsel," he recalled, adding that it continues to be the source of some confusion.

"That's just one small lesson on some of the challenges that can be faced when you have an element of financial statement reporting that is incorporated into the tax code," Desmond said, noting that Biden's minimum tax on corporate book income would have a much larger scale and would pose some challenges for the IRS in developing the necessary expertise to administer such provisions.

Desmond noted, for example, that restatements of financial statements are not uncommon, which then raises the question of whether the IRS would need to have the expertise to review financial statement reporting itself on top of looking at tax reporting. "I think there's an important role for looking at financial statement reporting, but I think we need to be cautious about incorporating that more wholesale into a bottom-line computation of tax liability," he said.

Wong acknowledged that Biden's proposal poses implementation challenges, but she argued that the cost of not making such changes, particularly for the purpose of raising revenue to finance investments in infrastructure and renewable energy, would be high. "These absolutely require federal revenue," she said, noting also there's broad public support for raising taxes on the wealthy and corporations.

"We are talking about trying to reverse a race to the bottom, not just internationally, but also domestically," Wong said.

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