THE NEW ENGLAND COUNCIL

Committee Update

April 11, 2013

President Obama's FY 2014 Budget Proposal
Financial Services Sector

On Wednesday, President Obama released his delayed 2014 budget proposal, completing the initial phase of the federal budget process. In recent weeks, both House and Senate have passed vastly different budget resolutions, with each chamber heavily influenced by the respective majority. These differing budget resolutions set broad parameters for the more detailed appropriations processes occurring in both House and Senate over coming months. The White House budget proposal describes the President's priorities and ideas for the spending and revenue targets in 2014. While largely symbolic, the President's budget does signal areas of budget emphasis early in the negotiating process with Congress.

With respect to the financial services sector, the President's budget included a number of significant policy elements, including the widely rumored proposal to cap tax-deferred savings in individual retirement plans at $3 million in total savings. According to the Administration, the proposal will generate over $9 billion in additional revenue over the next ten years. Beyond negative industry reaction, the proposal also drew fire from retirement savings experts and retiree advocates who criticized coupling a cap on private retirement savings with proposed changes to Social Security and Medicare benefit calculations. Critics of the retirement savings cap also emphasized the potential impact on younger workers saving over time as interest rates potentially rise. According to the Employee Benefit Research Institute (EBRI), only around 0.06 percent of total IRA account holders had $3 million as of the end of 2011, and 0.0041 percent of 401(k) accounts had $3 million as of the end of 2012. However, as interest rates rise, a growing number of savers would be affected. EBRI estimates that the currently proposed $3 million cap would more likely translate into a $2.2 million cap when interest rates return to historical levels, and affect up to six percent of younger workers who are now between the ages of 26 and 35. Obama's budget also proposes requiring that non-spouse beneficiaries of IRAs and 401(k)s distribute all money received within a five-year period, rather than over a lifetime.

For large banks and financial institutions, the president proposed a new "Financial Crisis Responsibility Fee," to be levied on institutions based on size and perceived risk. The fee is intended "to fully compensate taxpayers for the support they provided to the financial sector during the 2008–2009 economic crisis and to discourage excessive risk-taking" in the future, according to the budget text. This proposal is projected by the Administration to raise nearly $60 billion in revenue.

The Obama budget includes a new method of taxing derivatives, a proposal that actually originated with House Ways and Means Committee Republicans. This would require “mark to market” accounting on derivative contracts, requiring investors to pay taxes on unrealized gains from derivatives. This change is projected to raise more than $19 billion over the next decade.

In terms of corporate tax reform proposals, calling for a “revenue-neutral” approach Obama proposed overhauling the routinely passed tax “extender package” to finance lower overall corporate tax rates and a simplified system. White House officials have said the administration remains committed to lowering corporate tax rates from 35 percent to 28 percent, but that target was not clearly identified in the budget proposal. The President budget also omitted the issue of moving to a territorial tax system. For details about the current Administration thinking about corporate tax reform, please click here.

In the area of personal taxes, the President re-proposed implementation of the so-called “Buffet Rule” for those with adjusted gross income of more than $1 million, creating an average tax rate for those in this group of 30 percent. He also proposed limiting the maximum value for itemized tax deductions for those paying taxes above the 28 percent bracket. This would include deductions such as mortgage interest, charitable contributions, municipal bonds and state and local taxes. The President budget also includes a provision that would tax “carried interest” from investment funds as ordinary income rather than at the lower capital gains rate. Finally, he would raise the estate tax to 45 percent and reduce the standard deduction for married couples from $10.3 million to $3.5 million.