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Senate tax reform bill crosses finish line after major rewrite

The Senate voted almost entirely along party lines to approve its version of comprehensive tax reform legislation December 2, but not before Republican leaders made some significant modifications to win support from wavering members within their own ranks.

As approved, the modified Senate version of the Tax Cuts and Jobs Act (H.R. 1), which cleared the chamber by a vote of 51-49, follows the broad contours of the measure that was reported out of the Senate Finance Committee on November 16 by providing permanent tax relief – including a significantly lower top rate – for corporations and temporary tax relief for individuals and passthrough entities, with those costs offset in part by eliminating or paring back dozens of current-law deductions, credits, and incentives.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/171201_1_suppA.pdf

Protecting a fragile majority

Congressional Republicans opted to move tax reform legislation under budget reconciliation protections, which allow for passage in the Senate by a simple majority vote rather than the three-fifths supermajority normally required to clear procedural hurdles in that chamber, making it a particularly useful tool for Republicans, who control only 52 Senate seats and who did not expect – and did not receive – any Democratic support.

But in the weeks since the bill was approved in the Finance Committee, it was unclear whether Republican leaders would be able to secure the bare minimum of 50 votes from their own conference members to clinch a victory on the Senate floor (with Vice President Mike Pence stepping in as a potential tiebreaker) as a growing number of GOP lawmakers weighed in with concerns on a range of issues such as the treatment of passthrough entities, the proposed repeal of the individual mandate under the Patient Protection and Affordable Care Act, and the measure's long-term impact on the federal deficit. That led to an intense period of negotiations as leaders sought to extinguish one set of fires without sparking new ones elsewhere within the conference.

This report offers a high-level overview of some of the more significant modifications in the revised bill.

Proposed corporate rate holds at 20 percent

The revised bill, which was released late on December 1, retains provisions from the Finance Committee measure that would lower the top corporate tax rate to 20 percent beginning in 2019. An amendment offered on the Senate floor by Republican Sen. Marco Rubio of Florida to raise it slightly (by less than 1 full point) in exchange for a larger refundable child tax credit was subject to a point of order and fell far short of the 60 votes needed to overcome it.

Expanded passthrough, SALT benefits; higher repatriation rates

The revised bill would expand some tax benefits included in the Finance Committee legislation and add provisions that were not in the Finance package. But it also includes some potentially painful offsets affecting business and individual taxpayers.

Benefits: Notable changes intended to make the bill more attractive to certain senators would:

- Increase the deduction for passthrough business income to 23 percent (from 17.4 percent in the Finance Committee proposal). This change was made to win support from Republican Sens. Ron Johnson of Wisconsin and Steve Daines of Montana, who have been increasingly vocal in recent weeks about what they viewed as the inequitable treatment of passthrough entities in the Finance bill as compared to the rate reductions being provided to corporations.
- Incorporate a House bill provision allowing taxpayers to deduct up to $10,000 in state and local property taxes but repealing the deduction for state and local income taxes. (The Finance Committee bill called for repealing the deduction for state and local income, sales, and property taxes alike.) This provision received especially strong backing from Maine Republican Sen. Susan Collins.
- Permit a deduction in 2017 and 2018 for medical expenses exceeding 7.5 percent of adjusted gross income (AGI) – another Collins-backed provision. The current-law deduction is generally only for unreimbursed medical expenses in excess of 10 percent of AGI (7.5 percent for those age 65 or above).
- Retain current-law rules for domestic international sales corporations (DISCs). These would have been repealed under the Finance Committee bill.
- Modify the 100 percent expensing provision to phase down write-offs for business investments after 2022 rather than allowing the provision to immediately sunset.
- Retain tax-exempt status for professional sports leagues. (This would have been repealed under the Finance Committee bill.)

Offsets: On the revenue side, the revised bill includes provisions that, among other things, would:

- Retain the corporate alternative minimum tax (AMT) and a modified version of the individual AMT. (The Finance-passed bill would have repealed the AMT for individuals and corporations.)
- Increase the deemed repatriation tax rates to 7.49 percent for noncash assets and 14.49 percent for cash and cash-equivalents (up from 5 percent and 10 percent, respectively, in the Finance Committee bill and slightly higher than the 7 percent and 14 percent rates, respectively, included in the House-passed version).
- Sunset the suspension of the overall limitation on itemized deductions after 2024 rather than 2025 as proposed in the Finance Committee bill.

Nothing specifically for deficit hawks

The revised bill does not appear to include provisions that directly address concerns raised by Tennessee Republican Sen. Bob Corker and other fiscal hawks about long-term deficit effects.

Deficit issues threatened to upend progress on the Senate bill November 30 after the Joint Committee on Taxation (JCT) staff released a “dynamic” revenue score which estimated that the economic growth effects of tax reform would boost federal revenues by only $407.5 billion on a net basis between 2018 and 2027, reducing the bill’s net impact on the federal deficit over the 10-year budget window to just over $1 trillion, compared to $1.4 trillion for the same period under the JCT’s conventional “static” scoring method and $1.45 trillion under a preliminary static estimate released by the Congressional Budget Office. (Congressional Republican leaders and White House officials had argued in recent months that the economic growth resulting from tax reform would largely offset the cost of rate reductions and other tax relief over time.) And on the heels of the JCT’s news, the Senate parliamentarian ruled that a “trigger” provision sought by Corker that would claw back certain tax cuts if economic growth failed to hit certain benchmarks violates Byrd Rule prohibitions against reconciliation bill provisions that have no revenue impact or whose revenue impact is merely incidental.
URL: https://www.jct.gov/publications.html?func=startdown&id=5045
URL: https://www.jct.gov/publications.html?func=startdown&id=5043
URL: https://www.cbo.gov/system/files/115th-congress-2017-2018/costestimate/53362-summarysenatereconciliation.pdf

In the wake of those developments, Corker told reporters November 30 that he had worked out a deal with Senate Republican leaders to whittle $350 billion off the cost of the bill to retain his support. (Corker, Ron Johnson, and Arizona Sen. Jeff Flake of Arizona even threatened to vote with Democrats on a resolution to recommit the bill to the Finance Committee – a result that effectively would have scuttled the legislation – if there were no deficit concessions from leadership.)

As Republican leaders worked on a rewrite behind closed doors, however, they were able to win over enough holdouts and fence-sitters by making changes in other areas of the bill such as passthroughs (Johnson and Daines), business expensing (Flake), and deductions for state and local property taxes and medical expenses (Collins) to retain a majority without having to pare back the overall level of tax relief to secure the support of Sen. Corker, who subsequently announced he would oppose the legislation. (Corker turned out to be the sole Republican to vote against the measure.)

Floor amendments

The Senate considered a slew of amendments from the floor, most of which were defeated along party lines or ruled out of order. However, lawmakers did approve by a vote of 51-50 an amendment from Sen. Ted Cruz, R-Texas, that would allow funds from tax-preferred section 529 accounts – currently used to promote savings for college – to be used for costs associated with elementary and secondary education, including homeschooling. All 48 Democrats, plus 2 moderate Republicans (Susan Collins of Maine and Lisa Murkowski of Alaska) opposed the amendment and 50 Republicans voted in favor. Vice President Pence cast the tie-breaking vote.

The Senate also adopted, by a vote of 52-48, an amendment offered by Democratic Sen. Jeff Merkley of Oregon related to the new excise tax on college and university endowments. The substitute amendment unveiled December 1 included language authored by GOP Sen. Pat Toomey of Pennsylvania that would have exempted from that tax those educational institutions that forego certain forms of federal assistance. Although nominally available to any college or university, critics claimed it was designed to benefit a single school, Hillsdale College in Michigan. Merkley’s amendment to strike the exemption from the excise tax drew support from 4 Republicans and all 48 Democrats.

Next steps

The Senate-approved measure must now be reconciled with a competing version of the legislation approved in the House on November 16. House Republican leaders insist there will be a formal conference and have told members they will vote to initiate the conference on December 4.

Among the most significant differences still remaining between the two bills that will have to be worked out are the base-erosion prevention provisions that apply to international business activity; the proposed treatment of passthrough entities; the individual rate structure (four brackets in the House plus a bubble rate versus seven in the Senate); the treatment of the estate tax (fully repealed in the House versus a temporarily larger exemption in the Senate); the treatment of mortgage interest (the House bill would cap the deduction for future mortgages at loan amounts of $500,000 while the Senate would retain the current-law cap of $1 million); and the taxation of certain life insurance company income (the House bill includes an 8 percent surtax).

Other differences in the two bills may be easier to reconcile, such as the Senate's proposed delayed effective date for the corporate rate reduction and the treatment of individual tax incentives for medical expenses and student loan interest. The House is also likely to be left with no choice but to accept the Senate's sunsets on the individual side of the code at the end of 2025, since they are necessary to making the budget math work for the Senate under the Byrd Rule (which prohibits reconciliation bills from increasing the budget deficit outside the applicable budget window), and Republicans are already making clear that the expiring provisions will be extended by a future Congress.

— Michael DeHoff, Jacob Puhl, and Storme Sixeas
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TCPI webcast: Tax reform – Set to cross the goal line? Or more roadblocks ahead?

Tax reform is dominating the headlines as proposals make their way through both the House and the Senate. How close is Congress to enacting tax reform legislation? And how might it impact your organization specifically?

In a special one-hour webcast sponsored by the Tax Council Policy Institute (TCPI), Jon Traub, managing principal for tax policy at Deloitte Tax LLP and a former staff director for the House Ways and Means Committee, will be joined by tax specialists and former senior Capitol Hill staffers from other Big Four accounting firms to discuss:

- The current state of tax reform;
- Proposed tax relief provisions, revenue offsets, and their potential impact on business and individual taxpayers;
- Procedures and timelines for getting tax reform enacted – and the likelihood of it happening by year end; and
- What taxpayers need to think about doing now to increase the benefit and limit the disruption if it is enacted.

Webcast details

This complimentary webcast will be held on Thursday, December 7 from 11:00 a.m. – 12:00 p.m., Eastern Time. One hour of CPE credit is available (administered by Deloitte Tax LLP).
Register for the webcast.
URL:
http://r20.rs6.net/tn.jsp?t=hkkbi58ab.0.0.kca7kqbab.0&id=preview&r=3&p=https%3A%2F%2Fevent.on24.com%2Fwcc%2Fr%2F1560842%2F6A06FA10691CB6C77E3EAFC62A546F6A

— Michael DeHoff
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