In this issue:

Trump speech offers few surprises – and fewer details – on tax, health care reform

President Donald Trump's address to a joint session of Congress on February 28 laid out tenets of tax reform and health care reform that broadly comport with plans currently being advanced by House Republican leaders; but the speech did not provide specific policy directives in some key areas where GOP lawmakers are struggling to reach consensus.

Tax reform

Trump clearly echoed calls from the congressional Republican playbook when he stated that his administration is developing "historic tax reform that will reduce the tax rate on our companies so they can compete and thrive anywhere and with anyone" as well as "provide massive tax relief for the middle class." Less clear, however, was his position on the hot-button issue of the border-adjustment tax proposed by House Speaker Paul Ryan, R-Wis., and Ways and Means Committee Chairman Kevin Brady, R-Texas, in the tax reform blueprint they released last June.
URL: http://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf

The blueprint proposes to move the US from its current worldwide tax regime to a territorial system for taxing domestic multinationals and to implement a new destination-based cash flow tax (DBCFT). Specifically, the DBCFT provides for "border adjustments" through a not-yet-specified mechanism that would serve to eliminate US tax on products, services, and intangibles exported abroad (regardless of their production location) and impose a 20 percent US tax on products, services, and intangibles imported into the US (also regardless of production location).

This border-adjusted tax – which has not yet been released as a discussion draft or an introduced bill and is described only in general terms in the House GOP blueprint – has become the focus of an intensive lobbying battle within the business community, with retailers, oil refiners, and other import-dependent industry sectors on one side and export-heavy businesses on the other. A number of Senate Republicans have also signaled their concerns about – or, in some cases, outright opposition to – the proposal, creating an uphill path for supporters. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 7, Feb. 17, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170217_1.html

For weeks, stakeholders have been looking for a clear signal from the president on whether or not he supports the House Republican proposal. In some media interviews, Trump has appeared to dismiss the proposal as "too complicated," but in others he has suggested that it remains under discussion as an option for tax reform. Treasury Secretary Steven Mnuchin, meanwhile, indicated in a Fox News interview on February 26 that the administration is looking at a "reciprocal tax" – something apparently distinct from the House GOP proposal – that is intended to ensure "that other countries treat us the way we're treating them."

The White House raised expectations of a definitive answer in early February when press secretary Sean Spicer said the administration would soon release "the outline of a comprehensive tax plan." The president has made similar mentions in the weeks since, but congressional anticipation of a detailed document appears to have been tempered.

In his address to Congress, Trump touched only broadly on border tax issues, calling for "a level playing field for American companies and workers" and noting that "when we ship products out of America, many other countries make us pay very high tariffs and taxes – but when foreign companies ship their products into America, we charge them almost nothing."

This passage was not contrary to the language used in recent months by Speaker Ryan and Ways and Means Chairman Brady to sell their congressional colleagues on the border-adjusted tax, but it stopped short of specifically advocating the House plan. When asked by a reporter shortly after the speech whether Trump had effectively endorsed the proposed border-adjusted tax, newly minted Commerce Secretary Wilbur Ross said, "No, he did not. What he addressed was the issue that needs to be solved, which is there's inequitable treatment of the US."

For now, Brady and Ryan continue to make the case for their proposal, and many others wait on legislative language to more fully assess the impact such a tax would have.

Across the Capitol, Sen. John Cornyn, R-Texas, a taxwriter and the majority whip, said March 2 that Senate Republicans are looking at alternatives to the border-adjusted tax because it remains "contentious."

"There are people working on other approaches because we definitely want to do tax reform," he told *Politico*. Cornyn added, "I think it would have difficulty passing in the Senate, and I think the White House is somewhat of two minds on the issue."

Despite the current pace of the legislative process, Treasury Secretary Mnuchin this week reiterated his belief that comprehensive tax legislation will be signed into law by August of this year.

"These are complicated issues and we're working through these complex issues, and we're going to get it done," Mnuchin said, adding that the administration is "working very closely with the House and the Senate and coming up with a combined plan."

Health care

On health care reform, President Trump used his speech to call for repealing the Patient Protection and Affordable Care Act (PPACA) and replacing it with a system that, among other things, would "help Americans purchase their own coverage, through the use of tax credits and expanded Health Savings Accounts" – a position generally consistent with the health care reform blueprint that House Republican leaders released in June of 2016 and the policy brief they released last month.
URL: http://abetterway.speaker.gov/_assets/pdf/ABetterWay-HealthCare-PolicyPaper.pdf
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170217_2suppA.pdf

Refundable credits a sticking point: However, a sticking point for some conservative Republicans in both chambers – and an issue that the president did not address – is whether or not these credits should be refundable.

A draft bill combining provisions from the House Ways and Means Committee and the House Energy and Commerce Committee – the two House panels with jurisdiction over health care legislation – includes a proposal for refundable tax credits, meaning individuals with little or no federal tax liability could receive more in tax credits than they owe in taxes. (The draft, which is dated February 10, 2017, was not officially released by either committee but has been circulating in Washington since February 24. Ways and Means Committee Chairman Brady has indicated that taxwriters continue to revise the measure as they consult with Congressional Budget Office staff regarding the potential budgetary impact of any proposed changes.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170303_1suppA.pdf

The draft in circulation outlines a schedule of refundable credits – based on age rather than income – that would be available to individuals who do not receive health insurance through an employer or a government program. Credits would start at $2,000 a year (for eligible individuals under 30), and increase by $500 dollars for every 10 years of age, to a maximum of $4,000 (for individuals over 60). Credits would be paid in advance on a monthly basis to taxpayers so that they could then purchase whatever insurance they like. According to the draft, a program would be established by January 1, 2020.

Leaders of the House Freedom Caucus and the House Republican Study Committee have criticized the refundable tax credits as a new form of entitlements. Freedom Caucus Chairman Mark Meadows, R-N.C., also objected to basing the credits on age without taking income into consideration.

"You can be a millionaire and not have employer-based health care and you're going to get a check from the federal government," he told reporters this week.

For his part, Republican Study Committee Chairman Mark Walker of North Carolina said that "in [its current] form, and absent substantial changes, I cannot vote for the bill and, in good conscience, cannot recommend RSC members vote for it either."

In the Senate, Republicans Rand Paul of Kentucky, Mike Lee of Utah, and Ted Cruz of Texas have also expressed opposition to the notion of a refundable health care tax credit.

Paying for repeal: Missing from Trump's speech was a discussion of how to offset the cost of the tax credits and nontax benefits of a PPACA replacement plan (such as guaranteed coverage for individuals with pre-existing conditions). The draft House bill calls for reducing the current-law penalties under the individual and employer mandates to zero and repealing the bulk of the taxes that provide PPACA's revenue stream. It does, however, propose to fund the credits by creating a "cap" on the income exclusion for the value of employer-provided health care under a new Internal Revenue Code subsection 106(h). (Currently, the exclusion from income of employer-provided health care is the largest tax expenditure in the tax code.)

According to the draft, the cap would function by setting a threshold above which any health care benefit provided by an employer would be added to the employee's gross income, rendering it taxable. This "annual limitation" would be "equal to the 90th percentile of annual premiums" for calendar year 2019 and would then be indexed for inflation for years after 2020.

Similar to the disagreement over refundable credits, some conservatives see this cap as problematic. Meadows expressed concern that this threshold would cause the number of taxpayers subject to the exclusion to fluctuate with premium costs from year to year. Several GOP lawmakers also drew comparisons to the PPACA's "Cadillac tax," which would levy a 40 percent excise tax on employer-provided plans whose costs exceed a certain threshold. (The Cadillac tax, which is not set to take effect until 2020, would be repealed under the draft House bill.)

Republican Sen. Rand Paul told reporters March 1 that he is "completely opposed" to capping the exclusion.

"[T]hat's the 'Cadillac tax,' and basically that's a Democrat idea," Paul said. "I don't want a bunch of Democrat ideas dressed up in Republican clothing and stuck into the repeal bill. Let's vote for repeal."

Ways and Means Chairman Brady confirmed to reporters on March 2 that his panel is “looking at” a cap on the exclusion for employer-provided health insurance as one option to offset the cost of the tax credits and expanded access to health savings accounts; but he cautioned that “those are the final policy decisions we have not reached.” He also brushed aside comparisons between the proposed cap and the Cadillac tax, saying that the two differ “in about a dozen ways.”

Moving forward: Press reports indicate that the Ways and Means and House Energy and Commerce committees could mark up their respective PPACA repeal-and-replacement bills the week of March 6, although nothing had been officially announced by either panel at press time.

Budget reconciliation: A powerful, but complicated, procedural tool

Assuming that Republicans resolve their current policy disagreements, congressional GOP leaders have discussed the possibility of moving both a PPACA repeal-and-replacement bill and tax reform legislation under so-called “budget reconciliation” protections, which essentially would allow them to push those measures through the House and Senate without Democratic support.

But even though reconciliation holds the promise of a fast-track legislative process, the complexities of the reconciliation rules potentially could create additional difficulties for the GOP in advancing such a massive agenda.

Impact on PPACA repeal: The fiscal year 2017 budget resolution that Congress approved earlier this year paves the way for PPACA repeal by including budget reconciliation instructions which direct relevant committees – i.e., the Finance and Health, Education, Labor, and Pensions committees in the Senate and the Ways and Means and Energy and Commerce committees in the House – to each report legislation that reduces the deficit by $1 billion over the next decade. (As a parliamentary matter, a budget resolution cannot stipulate specific policies to be reported, although as a political matter it is understood that the forthcoming bills will deal with dismantling the PPACA.) The House committee legislation, as already noted, could be reported out in the coming days.

As long as legislation moved under the reconciliation process complies with the given instructions and certain other procedural and budgetary rules, it can be passed through both chambers with simple majority votes – a potentially powerful tool for Republicans who control 52 seats in the Senate, where 60 votes are normally required to advance legislation under regular order.

But those procedural and budgetary rules are strict, and Republican efforts to comply with them will likely shape the contours of any final bill.

One better-known restriction on the reconciliation process is the so-called “Byrd Rule” prohibition against legislation that would increase the deficit in any year beyond the budget window, which is typically 10 years. (The Byrd Rule is named after the late Sen. Robert Byrd, D-W.Va.)

In the context of current discussions around the PPACA, this rule is relevant to Republican efforts to move certain “replace” measures (such as new tax credits and expanded Health Savings Accounts) along with repeal, particularly if the reconciliation bill also repeals the taxes that helped fund the coverage expansion under the original health reform law. This rule may have contributed the decision by House Republican leaders to propose a limit on the tax exclusion for employer-provided health coverage as part of the February 10 draft bill that has been circulating in the tax community.

Another constraint of the “Byrd Rule” prohibits the inclusion of provisions in a reconciliation bill that are deemed to have no effect on the federal budget, or whose effect is “merely incidental” to the underlying policy.

These two budgetary restrictions on the reconciliation process have been codified into law and apply on a provision-by-provision basis. They are enforced through points of order, which can be waived in the Senate by a three-fifths majority (i.e., generally 60 votes), but because Democrats are not expected to lend any support to the PPACA repeal and replace effort, compliance with these rules is considered a prerequisite by Republicans.

Impact on tax reform: Members of congressional Republican leadership have telegraphed publicly that they also intend to utilize the budget reconciliation process to move tax reform legislation later this year. Because, as a general matter, only one bill affecting revenue can be moved pursuant to a single reconciliation instruction, this subsequent action on tax reform would require Congress to adopt another budget resolution for upcoming fiscal year 2018 with additional instructions targeted toward tax reform – a necessity that could bring into relief some of the differing budget priorities of the Trump administration (for example, increasing spending on infrastructure and defense, holding harmless Medicare and Social Security beneficiaries) and congressional Republicans, who in recent years have coalesced behind budget plans that would seek to achieve balance within 10 years by way of substantial spending cuts to mandatory spending programs like Social Security and Medicare. (The fiscal 2017 bill laying the groundwork for PPACA repeal is a bare-bones document with placeholder numbers that was designed only to tee-up reconciliation; House Speaker Paul Ryan has promised that the fiscal 2018 plan will be a more traditional blueprint that lays out Republicans' long-term budget policy goals.)

It is also noteworthy from a timing perspective that congressional Republicans must complete work on their forthcoming PPACA reconciliation package *before* they adopt a fiscal year 2018 budget with instructions geared toward tax reform. That is because, as a parliamentary matter, the adoption of a subsequent budget resolution would supersede the fiscal 2017 plan, and would erase Republicans' ability to separately move health and tax bills in a manner that shields each from a likely Democratic filibuster. (Republicans could, in theory, combine the two priorities into a single bill, but that would be a mammoth legislative undertaking that is currently considered unlikely to occur.)

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