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Border-adjustment tax gets mixed reviews from Ways and Means Republicans

House Ways and Means Committee Chairman Kevin Brady, R-Texas, stuck by his argument that a proposed border-adjustment tax would make US businesses more competitive internationally and remove current-law incentives for companies to relocate offshore in comments at a May 23 committee hearing. But even though most Republicans on the panel aligned themselves with Brady's position, other GOP taxwriters joined their Democratic colleagues in raising concerns about the proposal.

Border-tax overview

The "Better Way" tax reform blueprint that Brady and House Speaker Paul Ryan, R-Wis., released last June proposes a new destination-based cash flow tax that 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-adjustment 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 divided congressional Republicans and become the

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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.

Brady acknowledged the objections that have arisen in recent months, noting in his opening statement that "[w]e know there are legitimate concerns, including from some of our witnesses here today and our colleagues on the other side of the aisle about how it will affect American workers, businesses, and consumers. And we are committed to working with all of you to address these concerns. We have to get it right."

Impact on consumers

Several Republicans contended at the hearing that the proposal could have a detrimental impact – in the form of higher prices – on US consumers. Rep. Erik Paulsen of Minnesota, whose district is home to many Target Inc. employees – the retailer is headquartered in a neighboring district in downtown Minneapolis – said he "cannot support the border adjustability provisions as introduced last year in the blueprint."

Paulsen asked Target CEO Brian Cornell, who testified at the hearing, to elaborate on what he thought should be the key elements of any tax reform plan. Cornell replied that his top priorities were a lower rate as well as simplicity, clarity, and certainty – things that he said the border-adjustment tax would not guarantee.

"As I've listened this morning to the discussion, there's one word I continue to hear repeated again and again, and that's 'if.' *If* currencies appreciate, and *if* the GDP grows, and *if* manufacturing comes back, and *if* we can avoid trade wars. We certainly need to be sitting here working on something that's going to provide greater certainty to…the families we serve at Target, my 320,000 employees, [and] those small businesses that are in the back of the room," he said.

Rep. Jim Renacci, R-Ohio, said he is skeptical of the border adjustment but was trying not to be. He expressed his concerns as three questions: whether border adjustability picks winners and losers, who bears the ultimate burden of the tax, and whether it complies with our current international treaty obligations.

He said the first two questions can only be answered with economic theory at the moment. As to the third question, Renacci said that "at best, border adjustment is a case of first impression, and at worst it's a flagrant violation of our obligations."

Another GOP taxwriter seen as uncertain about the proposal was Mike Kelly, R-Pa., who asked witnesses how it would affect "the price on the shelf" and how it would affect consumers going forward.

Cornell replied that the supply chains for many consumer goods currently do not exist in the US and cautioned that "unintended implications" of the border-adjustment tax could lead to higher prices on "essential" consumer items such as apparel and produce. He contended that lawmakers need to ensure they understand the impact of their proposals on consumers as they move forward with tax reform.

Also among the unconvinced is Ways and Means Committee Republican Pat Tiberi of Ohio, who did not attend this hearing but weighed in with reservations about the proposal's impact on consumers at a May 24 committee hearing to examine President Trump's budget and tax reform proposals.

Democrats on the panel argued that the tax benefits in the House GOP blueprint are generally skewed toward wealthier taxpayers and that an additional increase in consumer prices resulting from a border-adjustment tax would further squeeze low- and middle-income taxpayers.

"When you have shocks to an economy like trade disruption, technological change, and other things, you want the tax system to sort of insulate people from shocks so that everyone's after-tax income can go up," said Rep. Loretta Sanchez, D- Calif. "A rising tide should raise all boats."

Currency adjustment

One leading defense of the border adjustment has been an economic argument that currency will adjust to mitigate the effects of a tax on imports. Cheaper exports will lead to increased demand for US products and thus US dollars,

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which will drive up the currency enough that US businesses that purchase imported goods will have increased buying power that will offset increased purchase prices.

But not all lawmakers were sold on the idea that currency would adjust completely (that is, enough to cover the full burden of the tax on imports), let alone fast enough to mitigate the increased cost of imports. Renacci, for example, commented that "market analysts and currency experts have been skeptical; Wall Street firms believe there is a large potential for disruption and could cause volatility in the market."

Rep. Kenny Marchant, R-Texas, asked several witnesses how companies have fared in recent months with the dollar and euro fluctuating against the pound. Cornell of Target said that contracts for imports are often dollar-denominated, which negates a currency adjustment.

Another witness, Lawrence Lindsey, a former advisor to President Reagan, countered that the market power of large retailers and their ability to hedge for currency risk would allow them to adjust to a border tax.

"All the…countries that have border adjustability still have retail sectors…that haven't been wiped out by the imposition of border adjustability," he said.

WTO compliant?

Members on both sides and several witnesses expressed concern that a border-adjustable tax could run afoul of World Trade Organization (WTO) rules and potentially lead to the imposition of retaliatory tariffs. The general principle is that border adjustments are allowed in indirect taxes, such as a value-added tax (VAT), but not in direct taxes, such as an income tax. While many members compared the proposed border-adjustment tax to a VAT, others noted it is still technically an income tax levied on corporations based on where sales occur and not a consumption tax levied on consumers.

On the other hand, some members and witnesses advocated for a wait-and-see approach. In response to concerns expressed by Rep. Renacci, Lawrence Lindsey asserted that "no one will know until [the case] is brought [to the WTO]."

Ways and Means Tax Policy Subcommittee Chairman Peter Roskam, R-Ill., who supports the proposal, commented that "[i]t's important to recognize that [WTO] Director General Roberto Azevêdo has noted that there's lots of gray areas in the WTO rules and he has declined to speculate."

Another witness, Kimberly Clausing, a professor of economics at Reed College, said she was confident, based on conversations with trade lawyers that the WTO would find against a border-adjustment tax. She also noted in her answer to a question about WTO retaliation from Rep. Mike Thompson, D-Calif., however, that the dispute resolution provisions which could be triggered by a border tax are provisions the US negotiated and often protect US products in disputes.

Transition rules

Even those in support of border-adjustment tax agreed that transition rules will be necessary to avoid market shocks. Roskam said "a smooth transition is key," and in his closing remarks, Ways and Means Chairman Brady called for a "thoughtful, deliberate transition."

California Republican Rep. Devin Nunes asked former Reagan advisor Lawrence Lindsey for recommendations on phasing in the tax. Lindsey suggested that one approach would be to apply the tax initially to a percentage of imports and then gradually increase that percentage over time until the tax is fully phased in.

Better ways than the Better Way?

For their part, most Democrats on the panel argued that increased spending on infrastructure and education would do more to build the middle class and create jobs than transitioning the corporate income tax towards a consumption tax.

Ranking member Richard Neal, D-Mass., stated in his opening remarks that meaningful investments in infrastructure "can be done through the tax code and would also jump-start economic growth and create thousands of jobs." Neal

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added that "to remain competitive, we must invest in workforce development" to close the education and skills gap. He also expressed support for "using repatriation dollars to pay for infrastructure and/or other productive purposes for the middle class."

Rep. Mike Thompson of California argued that a lack of skilled workers – not a lack of capital formation – was the main impediment to economic growth in many states.

Several members also made the argument that it was disparities among labor markets and regulations rather than issues with the US tax code that has caused production of many goods to move overseas. Citing examples of industries leaving the US for China and Mexico, Rep. Sander Levin, D-Mich., argued "it wasn't because of our tax systems; it was because of the huge differential in the cost of labor."

The Trump administration, meanwhile, has yet to fully embrace or reject the notion of a border tax. Treasury Secretary Steven Mnuchin has stated that the proposal "does not work in its current form" although the administration likes "some parts" of it. But in comments at a May 23 forum sponsored by the Peter G. Peterson Foundation, Mnuchin appeared to criticize the proposal more directly, saying that it "doesn't create a level playing field for all US businesses" and that "it has very different impacts on different companies, ...the potential to pass on significant costs to the consumer, [and]...the potential of moving the currencies."

White House budget prompts more border tax discussion

The border-adjustment tax was also one of several topics addressed at a House Ways and Means Committee hearing on the president's budget and tax reform proposals on May 24 and a Senate Finance Committee hearing covering the same ground on May 25. Treasury Secretary Mnuchin was the sole witness at both hearings. (See separate coverage in this issue for details.)

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Trump budget offers no new tax reform detail

The fiscal year 2018 budget package that President Donald Trump sent to Congress this week contains little new information on the administration's plans to reform the tax system – and House and Senate taxwriters were largely unable to suss out significant additional details from Treasury Secretary Steven Mnuchin when he discussed the tax-and-spending blueprint at two subsequent committee hearings.
URL: https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/budget/fy2018/budget.pdf

Restatement of 'principles'

The tax policy discussion in the administration's budget proposal, which the White House released on May 23, is mostly limited to a general reiteration of many of the tax reform "principles" laid out in the one-page fact sheet it unveiled last month. Those principles include, among other things, lowering rates on individual and business income, shifting to a territorial system for the taxation of foreign-source income of US multinationals, and eliminating unspecified "special interest" tax breaks. But the fact sheet does not address certain high-profile proposals in the tax reform blueprint released by House Republicans last June, such as a border-adjustment tax on products and services imported into the US, 100 percent first-year expensing, and repeal of the deduction for net corporate interest expense. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 14, Apr. 26, 2017 and *Tax News & Views*, Vol. 18, No. 15, Apr. 28, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170426_1.html
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170428_1.html

The budget does, however, propose two discrete tax policies outside the context of comprehensive tax reform (i.e., requiring taxpayers to provide valid Social Security numbers in order to receive the child tax credit and increasing oversight of paid tax return preparers) and also – as expected – calls for repealing the Patient Protection and Affordable Care Act (which the budget notes would reduce federal revenues by $1 trillion over the next decade).

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Ambitious fiscal goals

At a high level, Trump's budget seeks to achieve balance by 2027 (the last year of the 10-year budget window) through a mix of major cuts to nondefense discretionary spending, entitlement programs such as Medicaid, disability insurance, and food stamps (now called the Supplemental Nutrition Assistance Program), reductions in retirement benefits for federal workers, and reduced debt service costs. These spending reductions would be offset in part by proposed increases in defense spending and outlays on infrastructure.

However, that ambitious fiscal goal has come under heavy scrutiny by some observers as it relies on an assumption that, on account of the budget's policy, real growth in gross domestic product accelerates from 1.9 percent at the end of last year to 3.0 percent by 2020 and holds steady at that level for the duration of the budget period (roughly a full percentage point above comparable projections by the Congressional Budget Office). This supposition generates some $2 trillion in savings over the next decade that are included in the budget's baseline revenue and spending levels.

Double counting?: It is against this baseline, then, that the budget proposes "deficit neutral" tax reform – a characterization that has led some critical observers to argue that the budget must be either double-counting the additional revenue it expects from the growth effects of its tax reform plan (once for helping achieve a balanced budget, and a second time for helping offset the cost of the president's proposed tax rate reductions) or, alternatively, the administration is now switching course and proposing that its tax reform plan be revenue-neutral on the basis of conventional scoring which does not incorporate the feedback effects on revenue from changes in economic growth. The latter stance seems unlikely given Treasury Secretary Mnuchin's frequent commentary that economic growth will help offset the White House's proposed tax rate cuts, though White House Office of Management and Budget (OMB) Director Mick Mulvaney suggested this week that tax reform might be revenue neutral on a "static basis," meaning the administration would identify and support enough base broadening provisions to directly offset the revenue loss from lower marginal rates.

Former Treasury Secretary Larry Summers expressed his concern on the matter in a *Wall Street Journal* op-ed:

"You can't use the growth benefits of tax cuts once to justify an optimistic baseline and then again to claim that the tax cuts do not cost revenue," Summers wrote. "At least you cannot do so in a world of logic."

Too early for precise assumptions?: But OMB Director Mulvaney defended the administration's assumptions during a May 23 press briefing.

"I'm aware of the criticisms and would simply come back and say there's other places where we were probably overly conservative in our accounting. We stand by the numbers," Mulvaney said. "We thought the assumption that the tax reform would be deficit neutral was the most reasonable of the three options we had. We could either assume that tax reform was deficit neutral, we could assume it would reduce the deficit, or we could assume it would add to the deficit. And given the fact that we are this early in the process of dealing with tax reform we assumed that this middle road was the best [option]."

Treasury Secretary Mnuchin likewise commented in a May 23 interview on CNBC that the administration "felt it was premature to put in any changes to the budget as a result of taxes since we're not far enough along to estimate what that impact will be."

Mnuchin (largely) sticks to the script at taxwriting hearings

The preliminary nature of the administration's negotiations with House and Senate leaders on a tax reform agreement appeared to be reflected in many of the answers Mnuchin provided to tax policy questions he faced at a House Ways and Means Committee hearing on the president's budget and tax reform proposals on May 24 and a Senate Finance Committee hearing covering the same ground on May 25. Mnuchin was the sole witness at both hearings.

Border-adjustment tax: Mnuchin did little to elaborate on the administration's stance on a proposal in the House GOP tax reform blueprint that would impose a border-adjustment tax of 20 percent on all products and services imported into the US (regardless of where they are produced) and eliminate US tax on products, services, and intangibles exported abroad (also regardless of their production location). In the past, Mnuchin has stated that the proposal "does not work in its current form" although the administration likes "some parts" of it. In his May 23 comments at an event sponsored by the Peter G. Peterson Foundation, Mnuchin appeared to criticize the proposal

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more directly, saying that it "doesn't create a level playing field for all US businesses" and that "it has very different impacts on different companies, ...the potential to pass on significant costs to the consumer, [and]...the potential of moving the currencies."

At the Ways and Means hearing, however, Mnuchin responded to questions from Ways and Means Republican Pat Tiberi of Ohio and Democrat Lloyd Doggett of Texas – who both expressed reservations about the border-adjustment tax – by reiterating that he has "concerns" with the proposal and is "working very closely" with Ways and Means Chairman Kevin Brady, R-Texas, to address them. When Doggett asked whether the administration would offer specific changes to the proposal or was relying on taxwriters to develop an acceptable fix, Mnuchin replied: "I don't think it's our job to fix it."

When Doggett asked how the administration would close the $1 trillion revenue gap that would result if the proposal were left out of an eventual tax reform plan, Mnuchin stated only that the administration was considering "lots of different scenarios."

When Ways and Means Republican Tom Rice of South Carolina – who supports the proposal – subsequently posed the same question, Mnuchin commented that "many other countries...have a VAT tax system and a corporate tax system and use them in conjunction."

Mnuchin did not dangle the prospect of a value-added tax when Nevada Republican Sen. Dean Heller asked about alternatives to a border-adjustment tax during the May 25 Finance Committee hearing, however. Instead, he stated only that the administration is "looking at everything" and that "nothing is off the table."

(House taxwriters also held a separate hearing on May 23 to explore the impact of the border-adjustment tax on promoting economic growth and making US businesses more competitive internationally. See separate coverage in this issue for details.)

Depreciation and corporate interest expense: Lawmakers on both committees pressed Mnuchin about the administration's stance on issues regarding cost recovery and the tax treatment of business interest expenses. Responding to a question from Ways and Means Republican Jim Renacci of Ohio, Mnuchin stated that he would prefer to retain the current-law deduction for corporate interest expense, although the administration continues to consider all base-broadening options as it looks for ways to offset the cost of a business rate cut. (Mnuchin recently indicated in an interview in *The Economist* that he is "contemplating" keeping the interest expense deduction rather than scrapping it.)

Under the House Republican blueprint, interest expense would be deductible against interest income, but no current deduction would be allowed for net interest expense. Net interest expense could be carried forward indefinitely and deducted against net interest income in future years. The provision is included in the blueprint as a tradeoff for a proposal that would allow 100 percent expensing in year one for all assets, tangible and intangible, other than land. Ways and Means Chairman Brady has contended that pairing repeal of the interest expense deduction with 100 percent first-year expensing is "probably the most pro-growth" piece of the blueprint.

The administration's tax reform proposals are silent on the issues of interest expense and cost recovery. At the Senate Finance Committee hearing, however, Mnuchin told Republican taxwriter Charles Grassley of Iowa that the administration does "not support slowing depreciation" and that the administration is "looking at various alternatives" on depreciation issues as it negotiates a tax reform agreement. When Grassley asked if the administration is considering the House blueprint's proposal to pair 100 percent first-year expensing with repeal of the deduction for corporate interest expenses, Mnuchin replied that it was "something we're looking at carefully," adding that small and mid-sized businesses have expressed concern about the potential loss of the interest expense deduction.

Passthrough tax rates: In response to a question from Ways and Means member Vern Buchan, R-Fla., Mnuchin said that he is "absolutely committed" to providing tax rate parity for corporate and passthrough businesses. (The administration's tax reform principles call for a 15 percent rate for corporations and passthroughs). Mnuchin also reiterated that the administration would provide anti-abuse rules to prevent wealthy individuals from recharacterizing wage income as more lightly taxed business income, although he did not elaborate on how those rules would operate.

Finance Committee ranking Democrat Ron Wyden of Oregon contended at his panel's hearing that the administration's passthrough proposal seemed ripe for abuse and stated that he was not reassured by Mnuchin's promise of

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forthcoming safeguards. Wyden urged the administration to propose specific anti-abuse rules quickly, commenting that "tax cheats thrive in the absence of clear enforcement principles."

Other business tax expenditures: For the most part, Mnuchin resisted efforts by taxwriters at both hearings to pin him down on the fate of specific business tax expenditures under an eventual tax reform bill, noting only that the administration is looking at a broad array of base broadeners in an effort to buy down the business tax rate. But in response to a series of rapid-fire, yes-or-no-questions from Ohio Democratic Sen. Sherrod Brown at the Finance Committee hearing, the Treasury secretary offered a glimpse of certain provisions that – for the moment, at least – do not appear to be under consideration for repeal. Those include the last-in, first out (LIFO) accounting rules, the New Markets Tax Credit, and the low-income housing tax credit. Mnuchin also said the like-kind exchange rules are "one of the many things that could be looked at" but that no decision has been made, and that the administration's "preference" is to keep the interest deduction for state and local bonds. He did not offer specific answers to Brown's questions regarding cash accounting or the tax treatment of insurance companies, however.

'Mnuchin Rule': Ways and Means Democrats Sander Levin of Michigan, Lloyd Doggett of Texas, and John Larson of Connecticut pressed Mnuchin to confirm that the Trump tax reform plan would not result in an "absolute tax cut" for the upper class – an assertion he first made shortly after he was nominated to serve as Treasury sectary and has since become known informally as the "Mnuchin Rule." (For prior coverage, see *Tax News & Views*, Vol. 17, No. 34, Dec. 2, 2016.)
URL: http://newsletters.usdbriefs.com/2016/Tax/TNV/161202_1.html

Mnuchin explained to Levin that the administration's "objective" is for tax reform to simplify the tax code and provide a tax cut for the middle class and that it is looking at cutting rates for upper-income individuals but also eliminating most of the deductions – other than those for mortgage interest and charitable giving – that these taxpayers currently enjoy.

Under similar question from Pennsylvania Democratic Sen. Bob Casey at the Finance Committee hearing, Mnuchin stated that the administration's proposal "has been and will be a middle-income tax cut"; but he cautioned that he was "not guaranteeing anything" about what will be in a final agreement that the administration is in the process of negotiating with House and Senate leaders.

State and local tax deduction: Ways and Means Democrat Bill Pascrell of New Jersey and Finance Committee Republican Dean Heller of Nevada expressed concerns at their respective hearings about the administration's proposal to eliminate the deduction for state and local taxes paid as a way to write down the cost of lowering the tax rate for individuals. Mnuchin replied that the administration believes "the federal government should get out of the business of subsidizing states," but added that the White House expects to work with lawmakers to develop transition rules aimed at easing the impact of such a proposal on taxpayers.

Permanent v. temporary reform: Several lawmakers at the Ways and Means hearing emphasized the importance of enacting permanent tax reform – which would provide certainty for corporate and individual taxpayers alike – rather than an unpaid-for rate cut that would have to be temporary in order to comply with budget reconciliation rules. Mnuchin stated that his "preference" was for permanent tax reform, but under questioning from House Republican taxwriter Dave Reichert of Washington, he hinted that the administration has not definitively ruled out the possibility of a temporary tax cut.

"Permanent is better than temporary, and temporary is better than nothing," he said.

Extended budget window?: Rep. Jim Renacci asked Mnuchin at the Ways and Means Committee hearing whether Congress should consider extending the window beyond 10 years in the yet-to-be-drafted fiscal 2018 budget agreement to make it easier for tax reform legislation to move under reconciliation fast-track protections in the Senate – an idea recently floated by Senate Republican taxwriter Pat Toomey of Pennsylvania.

Mnuchin commented that an extended budget window is "a very good idea to consider strongly." (OMB Director Mick Mulvaney made similar comments at a May 24 House Budget Committee hearing.)

Budgetary rules governing the reconciliation process – often collectively referred to as "Byrd Rules," named after the late Sen. Robert Byrd, D-W.Va. – include a prohibition against legislation that would increase the deficit in any year beyond the budget window (unless offset by other budgetary changes within the same legislative title). In recent

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years, congressional budget resolutions have been written to cover budget policy over a 10-year time span, which matches the period over which the Congressional Budget Office and Joint Committee on Taxation typically analyze legislation. But there is no statutory requirement that these budget blueprints cover a decade; for example, it used to be common practice for budget resolutions to cover only five years. (For additional discussion, see *Tax News & Views*, Vol. 18, No. 16, May 5, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170505_3.html

A clean debt limit hike by August

Stepping away from the tax policy realm, Mnuchin stated at the Ways and Means Committee hearing that it was "absolutely important" that Congress approve a "clean" increase in the federal debt limit before adjourning for the August recess.

Lawmakers suspended the federal debt ceiling through March of this year as part of the two-year budget agreement reached in October of 2015. Since the debt limit was reinstated in March, Treasury has resumed the practice of relying on certain "extraordinary measures" to forestall a default on the federal debt and had projected that a hard deadline for action to increase the debt limit would come sometime this fall.

OMB Director Mick Mulvaney, however, stated on May 24 that the deadline may have to be accelerated because of "slower than expected" federal tax receipts.

In recent years, efforts to raise the debt limit became complicated when certain hardline conservative Republicans – notably, the House Freedom Caucus – sought to extract concessions on spending policy in exchange for a debt-limit hike. But Mnuchin told the Ways and Means panel that "we can all discuss how we cut spending in the future and how we can deal with the budgets going forward," but "protecting the United States' credit [should be] the most critical issue."

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CBO releases score of House-passed ACA repeal bill

The nonpartisan Congressional Budget Office (CBO) on May 24 released its much-anticipated assessment of the American Health Care Act (AHCA) – legislation narrowly passed by the House aimed at repealing and replacing the Patient Protection and Affordable Care Act (PPACA) – that, generally speaking, hews closely to its analysis of a previous iteration of the bill.

Lower deficit...

In its report, CBO projects that the bill (H.R. 1628), which cleared the House on May 4, would reduce budget deficits by roughly $119 billion over the next 10 years – the net effect of slightly more than $1.1 trillion in reduced spending and $992 billion in lower revenues. On the spending side, the savings would be generated mainly by phasing out the PPACA's Medicaid expansion (as well as implementing other Medicaid changes) and by replacing the current-law refundable premium assistance tax credits which subsidize coverage in the nongroup market for low-income individuals with less generous age-adjusted premium assistance credits.
URL: https://www.cbo.gov/system/files/115th-congress-2017-2018/costestimate/hr1628aspassed.pdf

On the tax side, the revenue reduction would stem from the bill's elimination of most of the tax increases enacted as part of the PPACA to help finance that law's coverage expansion (including the 3.8 percent net investment income tax and the additional 0.9 percent Medicare payroll tax on high-income households, plus new industry levies targeted at medical device makers, health insurers, and manufacturers of branded drugs) as well as by further delaying the effective date of the so-called "Cadillac" tax on high-cost employer-provided health plans and reducing to zero the monetary penalties associated with violating the current-law health insurance coverage mandates that generally apply to individuals and employers. (For prior coverage detailing the bill as passed by the House, see *Tax News & Views*, Vol.

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18, No. 16, May 5, 2017. Revenue estimates of the tax provisions in the House-approved bill are available from the Joint Committee on Taxation staff.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170505_1.html
URL: https://www.jct.gov/publications.html?func=startdown&id=5000

The $119 billion in projected net savings in the House-passed bill compares to a previous CBO estimate showing $337 billion in deficit reduction – the difference being mainly attributable to the net effect of several changes made late in the House process that would allow states to waive out of certain PPACA regulatory requirements in certain circumstances, add funding for so-called "high-risk pools," and delay the effective date of the repeal of the additional Medicare payroll tax to 2023.

...But insured population would drop significantly

CBO's previous analysis of the bill had projected that, by 2026, 24 million fewer individuals would have health insurance coverage relative to current law – largely due to the law's repeal of the Medicaid expansion and neutering of the individual mandate. Despite the new provisions that would allow states to waive out of certain PPACA requirements – and perhaps offer less comprehensive, less expensive, plans – the CBO's latest analysis projects a similar drop of 23 million in the ranks of the insured within 10 years.

On to Senate, but then what?

The AHCA is being moved pursuant to a budget reconciliation instruction included in the fiscal year 2017 budget resolution adopted by Congress earlier this year. That instruction called upon the Ways and Means and Energy and Commerce committees in the House and the Finance and Health, Education, Labor, and Pensions committees in the Senate to each report legislation that reduces the deficit by at least $1 billion. (Although the legislative text of budget resolutions and reconciliation instructions cannot stipulate specific policy, it was understood that the follow-on legislation was to be targeted at dismantling the PPACA.)

Provided that legislation moved under reconciliation follows certain strict budgetary and procedural rules – including adhering to the reconciliation instruction itself – it can be approved by a simple majority in both chambers, making it a potentially powerful tool for Republicans, who control 52 seats in the Senate, 8 shy of the 60 votes normally required to advance legislation in that chamber under regular order.

In recent days House Speaker Paul Ryan, R-Wis., had indicated that he would not formally transmit the House-passed bill to the Senate out of an abundance of caution that the modified AHCA may not meet the $2 billion combined deficit-reduction requirement included in the House reconciliation instructions, which would have required House Republicans to consider amending the bill in a way that generated the requisite savings and voting on it again – a difficult proposition given the bill's razor-thin margin of passage.

The $119 billion in net savings projected by CBO, however, suggests the AHCA can be transmitted to the Senate without losing its legislative privilege.

Senate starting from scratch: That said, many senators have expressed deep reservations about the House-passed bill – particularly with respect to its swift roll-back of the Medicaid expansion (20 Republican senators represent states that opted to expand Medicaid pursuant to the PPACA). Also potentially problematic is the bill's restructuring of the premium assistance tax credits, which several moderate Republican senators regard as insufficiently generous.

Because of these and other concerns, the Senate intends to essentially work from scratch and produce its own bill. A working group of 13 Republican senators has been meeting frequently toward that end, but the content of any legislation and the timeline for unveiling it remain uncertain.

Senate Majority Leader Mitch McConnell, R-Ky., alluded to that uncertainty in comments to reporters on May 24.

"I don't know how we get to 50 [votes] at the moment. But that's the goal," McConnell said. "And exactly what the composition of that [bill] is I'm not going to speculate about because it serves no purpose."

Byrd Rules still apply: As they work to find consensus, Republican senators will also have to contend with additional procedural and budgetary rules that govern the reconciliation process – often collectively referred to as "Byrd Rules,"

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named after the late Sen. Robert Byrd, D-W.Va. – among them being a prohibition against legislation that would increase the deficit in any year beyond the budget window (which spans 10 years, in this case) and a separate rule designed to block provisions 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 with a three-fifths majority (that is, 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 in essence a prerequisite for Senate passage of the bill.

In practical terms, these rules will require senators to find budget offsets for any changes they might make to moderate the policy in the House bill (with respect to Medicaid or the premium assistance tax credits, for example). It has also been speculated that the House provisions allowing states to waive out of certain PPACA rules may not have a direct and discernible impact on the federal budget, in which case they could be stripped out by Senate Democrats.

Ways and Means clears amendments on separate track

Also this week, House taxwriters approved three tweaks to the AHCA that would: codify an existing regulation which allows veterans who are eligible for, but not enrolled in, Veterans Administration health care to access tax credits offered under current law and the tax credits provided by the AHCA when they take effect (H.R. 2372); permit individuals who are eligible for COBRA continuation coverage to access the AHCA's tax credits (H.R. 2579); and prevent the AHCA's monthly tax credits and the PPACA's current subsidies from being dispensed until the legal status of an eligible recipient can be verified (H.R. 2581). The measures are not included in the AHCA measure being sent to the Senate and are intended to move on a separate legislative track.

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Deloitte Tax LLP

A note on our publication schedule

The House and Senate will be out of session the week of May 29 as lawmakers adjourn for their Memorial Day recess. Barring unexpected developments on the tax policy front, the next issue of *Tax News & Views* will be published the week of June 5, when the legislative session resumes.

— Jon Traub
Managing Principal, Tax Policy
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