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Brady offers possible changes to GOP tax reform blueprint

As efforts by Republican congressional leaders and the Trump administration to develop a single tax reform plan continued largely behind closed doors, House Ways and Means Chairman Kevin Brady, R-Texas, this week outlined possible revisions to proposals in the House GOP tax reform blueprint released last summer that call for imposition of a border-adjustment tax and repeal of net interest deductibility.

Border-adjustment tax

In recent weeks, Brady has acknowledged the strong opposition from some industries – and from some fellow lawmakers – to the border-adjustment tax proposal and has said he and the House taxwriters were considering modifications to make the new concept more palatable.

Five-year phase-in: Speaking to the annual *Wall Street Journal* CFO conference in Washington on June 13, Brady said his “current thinking” on the controversial proposal (which would tax all imports into the US at 20 percent and exempt all exports from taxation) is to phase it in over five years, providing a softer landing for import-dependent sectors.

"Businesses need plenty of time to assess their current supply chain and decide what, if any, can return to the United States," Brady said. "And they want plenty of time to see how the dollar adjusts and at what level."

One of the arguments Brady, House Speaker Paul Ryan, R-Wis., and other advocates of the border-adjustment tax proposal have made is that implementation would lead to a stronger US dollar, making it less expensive to import goods and effectively cancelling out the higher tax on imports. However, opponents are concerned that exchange rates won't adjust enough to offset the tax, which would result in increased prices on imported goods and services for US consumers.

Initial responses to Brady's comments from groups that have been the most vocal critics of the proposal suggested that the modifications would not be enough to bring them on board. Americans for Affordable Products, a coalition of companies lobbying to kill the border-adjustment tax plan, said the phase-in "does nothing to change the harmful impact on consumers. It only delays the political consequences for lawmakers." And Heritage Action CEO Michael Needham said that "[p]hasing in flawed, unnecessary policy is not a solution; in fact, it is likely to create more problems than it solves."

A number of House taxwriters who have raised concerns about the proposal – many of whom indicated they were not aware Brady would propose modifications this week – said they appreciated the work being done by the Ways and Means chairman but would need to see more details before endorsing a phase-in.

Rethinking industry carve-outs: In addition to a five-year phase-in, Brady also suggested this week that there should be special treatment for sectors such as financial services, shipping, communications, insurance, and digitally-focused businesses, where cross-border transactions are more challenging to identify.

"[It's] hard to determine…where the border begins in the cloud," he admitted.

This comes as something of a surprise because Brady and Ryan have for many months rejected the idea of carve-outs or exemptions for particular sectors, but it seems to be further acknowledgement of the fact that the proposal currently has more opponents in Congress than Republicans can afford to lose on a tax reform vote. With the strong headwinds its faces, the two main reasons the border-adjustment tax hasn't been completely laid to rest are first, that no acceptable alternative has emerged to address base-erosion concerns inherent in Republicans' proposed move to a territorial tax system, and second, that the tax is estimated to bring in about a third of the revenue necessary to offset Republicans' desired corporate rate cut.

The nonpartisan Tax Foundation released an analysis following Brady's speech calculating that a border-adjustment tax with a five-year phase-in would raise just over $1 trillion in revenue between 2017 and 2026 while an immediate border-adjustment tax would raise more than $1.2 trillion over the same period.
URL: https://taxfoundation.org/border-adjustment-phase-in/

Net interest expense deduction

Addressing another contentious provision in the House GOP blueprint, Brady also this week briefly touched on a potential exception to the plan's proposed elimination of the current-law deduction for net interest expenses. The blueprint pairs repeal of that deduction with a provision allowing full expensing of business investments.

"I foresee an exemption for small businesses [from the repeal of the interest expense deduction] so they can take advantage of both," he said. "They often don't have access to capital markets."

Brady did not provide any further details of how "small business" would be defined or how such an exception would be implemented, however. He also mentioned an exemption for real estate purchases and utilities.

More cars for the tax reform train

Meanwhile, various groups of rank-and-file House members weighed in this week with their own views on what a tax bill should – or shouldn't – include.

Welfare reform: While they have not yet been able to reach an official consensus position among their three dozen or so members, leaders of the conservative House Freedom Caucus hope their group will play an outsized role in the tax debate this year. Rep. Mark Meadows, R-N.C., the chairman of the caucus, and Rep. Jim Jordan, R-Ohio, a co-founder, are pushing to tie aspects of welfare reform to tax reform, and Meadows is urging Republican leaders to cancel the scheduled August recess in order to give lawmakers additional time to complete work on tax reform and other legislative priorities.

Meadows said on June 9 that the caucus is still developing its own outline of a tax bill, but he indicated that it would likely not include the border-adjustment tax. Instead, Meadows said that including changes to the Supplemental Nutrition Assistance Program (food stamps) and Temporary Assistance for Needy Families (welfare) could raise $400 billion over 10 years as a partial offset for business rate reductions. In line with the Republican blueprint, Meadows said members of the caucus generally support a 20 percent corporate tax rate, a similar rate for passthrough entities, a 20-month repatriation holiday with a reduced tax rate of 8 percent, and an increased standard deduction for individual taxpayers.

Ways and Means Chairman Brady told reporters that while he supports welfare reform, he believes it should be tackled separately from tax legislation.

"I think let's stay focused on tax reform. Let's look for opportunities to advance welfare reform this session," he said. "One is about getting people back to work with real, good-paying jobs. The other is about making sure there are enough good-paying jobs for folks who are trapped in welfare."

House taxwriter – and Freedom Caucus member – David Schweikert, R-Ariz., echoed Brady's sentiments in comments to reporters.

"The pitch I'm going to make [to the Freedom Caucus] is that tax reform is such a big deal to the country and to the world, with the US being much of the world's economic engine. We need to focus on just getting this right," Schweikert said. "Big time tax reform is going to be the biggest thing any of us ever vote on. Tying externalities, no matter how important they are, just [makes] the votes more difficult."

Infrastructure: Adding to the chorus of voices directed at taxwriters, a bipartisan group of more than 250 lawmakers sent a letter June 13 to Brady and Ways and Means ranking Democrat Richard Neal of Massachusetts urging that tax reform include a long-term solution to the Highway Trust Fund (HTF) solvency challenges. The HTF funds federal surface transportation projects but, as a result of structural changes in the transportation landscape, is no longer a self-funding mechanism. The current funding stream is set to expire in 2020. The letter was spearheaded by Rep. Sam Graves, R-Mo., chairman of the House Transportation and Infrastructure Committee's Subcommittee on Highways and Transit, and Delegate Eleanor Holmes Norton of the District of Columbia, the subcommittee's ranking Democrat.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170616_1suppA.pdf

President Trump has hinted in the past that he might consider linking tax reform and infrastructure as a way to win support from congressional Democrats. Treasury Secretary Steven Mnuchin, however, appeared to rule out that possibility in comments made after the administration released its statement of tax reform principles in April. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 16, May 5, 2017.) More recently, Transportation Department Secretary Elaine Chao said at a June 15 House Appropriations Subcommittee hearing that White House discussions about a tax reform-infrastructure pairing have "receded."
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170505_2.html

Carried interest: Also addressing Brady and Neal, 22 Republican House members on June 13 sent a letter urging that any tax legislation maintain the current treatment of carried interest income, the share of profits paid to investment managers. Republican taxwriters have in the past generally pushed back on proposals to tax carried interest at ordinary income rates instead of at capital gains rates, but President Trump has called for such a change this year. The House Republican blueprint does not address carried interest, and Ways and Means Committee members have said it's one of the issues in tax reform that they are still working to resolve. Signatories of this week's letter argued that carried interest meets all the criteria of long-term capital gains and should not be viewed as a "loophole" in the tax code.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170616_1suppB.pdf

'Rules' are made to be broken

In other developments this week, Treasury Secretary Mnuchin sought to defend the Trump administration from Democratic allegations that its tax reform principles (released in April as a one-page fact sheet) would result in lower taxes for the wealthiest Americans.

Democrats have frequently cited a statement Mnuchin made in late November, shortly after he had been tapped for his current role, that there would be "no absolute tax cut for the upper class" – something that has become known informally among Democratic lawmakers 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

But in remarks before the House Appropriations Financial Services and General Government Subcommittee on June 12, Mnuchin distanced himself from the nickname and clarified that his original statement was "an objective" as opposed to a promise.

"I didn't name the rule," Mnuchin said several times, adding that the president advocates eliminating almost all personal deductions under tax reform, which would increase effective tax rates for those who itemize. Mnuchin would not definitely state that the president would veto a tax plan that included net tax cuts for the wealthiest individuals, however.

Tax reform, not tax cuts

In an appearance before the Senate Budget Committee on June 13, Mnuchin affirmed his commitment to the enactment of revenue-neutral tax reform legislation rather than an unpaid-for package of tax cuts.

"…[W]e need to make sure that if we have tax reform – which is not just tax cuts, but tax reform – that it's paid for and accounted for," he said.

The House GOP blueprint calls for tax reform that is revenue neutral under "dynamic scoring" rules, which take into account certain macroeconomic feedback effects of tax and spending legislation – a position that Senate Majority Leader Mitch McConnell, R-Ky., has consistently endorsed.

But some Republican lawmakers – including members of the House Freedom Caucus – have indicated that they would be willing to accept a tax bill that adds to the deficit. Because GOP congressional leaders want to move tax reform under fast-track budget reconciliation rules that, among other things, preclude legislation that would increase the deficit outside the 10-year budget window, an unoffset tax bill would have to be drafted to sunset in a way that would prevent any net out-year revenue loss, as was the case with the reconciliation tax cuts enacted in 2001 and 2003.

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Details on Senate health care bill remain under wraps

Work continued behind the scenes this week on the Senate version of legislation to repeal and replace the Patient Protection and Affordable Care Act of 2010 (PPACA), but a draft proposal or even a detailed outline have yet to emerge and Republican leaders have offered no clear indication of when a completed product will be available.

"We'll let you see the bill when we finally release it," McConnell told reporters June 13. "Nobody's hiding the ball here."

Senate Republicans have opted to develop their own version of a health care bill rather than amend the House-approved American Health Care Act of 2017 (AHCA), the Affordable Care Act repeal-and-replacement package that narrowly cleared that chamber early last month. The legislation is being drafted by a working group of 14 Republican senators and is not expected to be vetted in committee, although leadership has been meeting regularly with rank-and-file party members to discuss the process. As recently as last week, though, lawmakers characterized those

meetings as focusing largely on conceptual issues. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 20, June 9, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170609_1.html

Trump calls for more generous benefits

Senate Republican leaders, like their House counterparts, face the daunting challenge of drafting a measure that can win support from conservatives, who would prefer to shed all vestiges of the PPACA, and from moderates, who want to ensure that a new bill does not disadvantage older and less affluent individuals. Adding to the challenge is the fact that Republicans can only afford to lose two votes if they intend to get their bill through the chamber strictly along party lines. (Senate Democrats are expected to oppose the legislation and Republicans only hold 52 seats in the chamber.)

That balancing act came into sharper focus during a meeting between President Trump and a group of GOP senators at the White House on June 13 during which the president reportedly urged the Senate to pass legislation with more generous benefits than those provided under the House-approved AHCA. (Although the president praised the AHCA as "incredibly well-crafted" during a speech in the Rose Garden after its passage in the House on May 4, a number of its provisions, notably those rolling back the PPACA's Medicaid expansion and those allowing states to opt out of the PPACA's essential benefits coverage requirements have been sharply criticized. White House aides have indicated that the president wants the Senate to produce legislation that would be easier for the administration to defend.)

Senators at the meeting who, like Alaska Republican Lisa Murkowsi, represent states that participated in the Medicaid expansion program, told the president that rolling back Medicaid expansion too quickly would hurt too many low-income families.

"I reinforced that I think Medicaid expansion has been very important to the state of Alaska," Murkowski told reporters after the meeting.

Sen. Rob Portman, R-Ohio, who also would like a slower Medicaid rollback, told reporters that the president "talked about the need to take care of people."

An official within the White House has indicated Trump has not yet taken a firm position on Medicaid expansion, but according to sources at the meeting, Trump advocated for more robust tax credits to help lower-income families buy health insurance on the individual market.

But including more generous benefits could alienate conservatives such as Kentucky Republican Sen. Rand Paul, who told reporters on June 15 that he is "not willing to vote for new entitlement programs."

Revenue implications

Beefing up tax credits or slowing the rollback of the PPACA's Medicaid expansion also would have serious effects on the measure's bottom-line revenue score. Should the Senate opt to increase benefits above what the House bill provided, budget reconciliation rules (which prohibit legislation that increases the deficit in years beyond the 10-year budget window or that saves less over the next decade than does the House-passed bill – $119 billion) would likely require lawmakers to retain some of the taxes enacted under the PPACA – or at least delay their repeal – to offset the higher cost of the package. (Among the more contentious PPACA taxes are 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. The House-passed legislation would repeal most of these retroactive to the beginning of this year.)

But for many conservative groups, leaving any of the PPACA taxes intact is a nonstarter. In a June 13 letter to Finance Committee Chairman Orrin Hatch, R-Utah, Americans for Tax Reform and dozens of other activist groups urged GOP lawmakers to repeal the PPACA in full, including all taxes.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170616_2suppA.pdf

Senate Majority Whip John Cornyn of Texas told reporters June 14 that the issue of how to address PPACA taxes "remains to be decided."

Prospects uncertain for pre-recess floor vote

The apparent lack of progress in drafting a bill has cast some doubt on whether the Senate will be able to vote on a completed package before the Independence Day recess, the deadline recently set by Majority Leader McConnell. (The chamber's last scheduled working day before their week-long adjournment is June 30.)

Part of the challenge in meeting that deadline involves waiting for a revenue score from the Congressional Budget Office (CBO), although lawmakers reportedly have been attempting to move that process along by submitting discrete provisions to the CBO for scoring in advance.

McConnell has stressed the importance of holding a vote in June, so that the House and Senate would have the bulk of July to resolve differences in their respective proposals and potentially send an approved bill to the White House before they adjourn for the August recess. That schedule also could free up time for lawmakers to tackle other pressing issues such as the debt ceiling and tax reform.

But some Republicans appear less than optimistic about sticking to that timetable. Finance Committee member John Thune, R-S.D., told reporters June 14 that the odds of meeting McConnell's deadline were "probably 50-50." Majority Whip John Cornyn predicted action "next month," adding that "it's something we have to do before we leave for August."

House OKs targeted health care tax provisions

Across the Rotunda, the House this week voted largely along party lines to approve three targeted Republican-sponsored health care tax measures 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 House-approved American Health Care Act if they are enacted into law (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).

Passage of the three bills is part of the House GOP's long-term plan to modify the AHCA once it is enacted by adding provisions that for procedural reasons could not be included in the original reconciliation bill.

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Ways and Means OKs expansion of advanced nuclear power production credit

The House Ways and Means Committee on June 15 approved by voice vote legislation (H.R. 1551) that would expand the advanced nuclear power production tax credit by making it available to facilities that are placed in service beyond the current-law cut-off date and allowing public entities to transfer credits to an eligible project partner.

H.R. 1551 is sponsored by Ways and Means Committee Republican Tom Rice of South Carolina and includes among its cosponsors Democratic taxwriter Earl Blumenauer of Oregon. An identical companion bill (S. 666) has been introduced in the Senate by Republican taxwriter Tim Scott of South Carolina.

Placed-in-service limitation removed

Under current law, a qualifying advanced nuclear facility may claim a credit for production of electricity based on the ratio of the allocated capacity it receives from the Treasury Secretary to its rated nameplate capacity. Among other restrictions, the credit is limited to 6,000 megawatts of national capacity and is available only for facilities placed in service by December 31, 2020.

H.R. 1551 would modify the megawatt capacity limitation for purposes of the credit by requiring the Treasury Secretary to allocate any unutilized capacity first to facilities placed in service before 2021 (to the extent they did not receive an allocation equal to their full nameplate capacity) and then to facilities placed in service on or after January 1, 2021, in the order in which they were brought on-line.

Credit transfers allowed

The proposal also would allow qualified public entities to elect to forgo credits to which they otherwise would be entitled and transfer them to an eligible project partner. Qualified public entities are defined as (1) a federal, state, or local government; (2) a mutual or cooperative electric company; or (3) a not-for-profit electric utility which has or had received a loan or loan guarantee under the Rural Electrification Act of 1936. An eligible project partner under the proposal generally includes any person who designed or constructed the nuclear power plant, participates in the provision of nuclear steam or nuclear fuel to the power plant, or has an ownership interest in the facility.

Effective date and cost estimate

The provision requiring reallocation of unutilized national megawatt capacity limitation would be effective on the date of enactment; the provision allowing transfer of credits to eligible project partners would be effective for taxable years beginning after the date of enactment.

The Joint Committee on Taxation staff estimates the measure would reduce federal receipts by $16 million over 10 years.
URL: https://www.jct.gov/publications.html?func=startdown&id=5001

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