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## Congressional, White House negotiators drop border-adjustment tax from tax reform principles

Congressional Republican leaders and White House officials announced in a joint statement July 27 that as part of their shared commitment to tax reform, a border-adjustment tax will not be included in any tax code overhaul that moves through Congress this year.
**URL:** https://www.republicanleader.senate.gov/newsroom/press-releases/joint-statement-on-tax-reform

The statement – which was released by House Speaker Paul Ryan of Wisconsin, Senate Majority Leader Mitch McConnell of Kentucky, House Ways and Means Committee Chairman Kevin Brady of Texas, Senate Finance Committee Orrin Hatch of Utah, Treasury Secretary Steven Mnuchin, and National Economic Council Director Gary Cohn (known informally as the "Big Six") – outlines a consensus Republican view of the key principles that should animate tax reform.

### 'Many unknowns' on border-adjustment

The statement is drafted in broad strokes and largely avoids specific policy details such as target tax rates for businesses or individuals. On the issue of corporate taxation, however, the drafters express confidence that "without transitioning to a new domestic consumption-based tax system, there is a viable approach for ensuring a level playing field between American and foreign companies and workers, while protecting American jobs and the US tax base."

"While we have debated the pro-growth benefits of border adjustability, we appreciate that there are many unknowns associated with it and have decided to set this policy aside in order to advance tax reform," the statement said.

The "Better Way" tax reform blueprint that Ways and Means Chairman Brady and House Speaker Ryan released in June of last year called for a new destination-based cash flow tax with "border adjustments" through an unspecified 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).

The concept of a border-adjustment tax – which is described only in general terms in the House GOP blueprint and was never fleshed out in a discussion draft or an introduced bill – had divided congressional Republicans and became 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. It also received only lukewarm support from President Trump.

**No alternative put forward**

The border-adjustment proposal in the blueprint has been unofficially estimated to raise over $1 trillion dollars to offset the cost of a corporate rate cut. Significantly, the statement does *not* propose any alternative revenue source for bankrolling a rate reduction.

**Other principles in brief**

In addition to discussing the border-adjustment issue, the statement from the Big Six also addresses some other significant tax reform priorities for businesses and individuals, albeit obliquely.

**Rates:** The statement calls for tax reform that "protect[s] American jobs and make[s] taxes simpler, fairer, and lower for hard-working American families" and lowers tax rates for businesses of all sizes "as much as possible."

**Permanence:** The statement urges the congressional taxwriting committees to develop legislation that "places a priority on permanence." This appears to be a call for lawmakers to move forward with comprehensive, revenue-neutral tax reform rather than a tax cut-only bill (which would have to be temporary in order to comply with the budget reconciliation rules, which preclude legislation that increases the deficit outside of the 10-year budget window).

**Territoriality:** The statement does not include an explicit call to adopt a territorial system for taxing foreign-source income of US multinationals. It does, however, call for tax reform that "creates a system that encourages American companies to bring back jobs and profits trapped overseas." The House GOP tax reform blueprint advocates a territorial tax system; Treasury Secretary Mnuchin commented at a July 26 Senate Appropriations and General Government Subcommittee hearing that moving to territoriality is a "main priority" of the Trump administration; and Finance Committee Chairman Hatch has been extolling the virtues of a territorial tax system in recent speeches and materials released by his panel.

**Cost recovery and limits on interest deductibility:** The statement includes a reference to "unprecedented capital expensing" for businesses; however, it does not specify the extent of any proposed change in the expensing rules nor does it mention pairing that proposal with changes to the treatment of interest deductibility.

The House GOP blueprint proposes 100 percent expensing for all assets – tangible and intangible – in year one, but pairs that provision with a call for repealing the deduction for net interest expenses. Small-business owners have argued that eliminating the deduction for net interest expenses could be problematic for businesses that rely on debt financing because they have limited access to capital.

**Handoff to the taxwriting committees…**

With the release of the statement, the Big Six appeared to shift the tax reform process back to the taxwriting committees, saying, "[o]ur expectation is for this legislation to move through the committees this fall, under regular order, followed by consideration on the House and Senate floors."

Regular order should include passage of the bills through both the Ways and Means and Finance committees before moving to the House and Senate floors, with the opportunity for members of both parties to offer amendments. This does not appear to preclude the use of the reconciliation process, by which Republicans could pass the legislation in the Senate with a simple majority vote rather than the three-fifths majority typically required for nonreconciliation bills to clear procedural hurdles in that chamber.

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