In this issue:

Senate Republicans, Democrats cement partisan split on tax reform

Senate Majority Leader Mitch McConnell, R-Ky., this week announced that the Senate likely would pursue a Republican-only tax reform plan under budget reconciliation rules after Democrats laid out their conditions for participating in bipartisan discussions. Meanwhile, Republicans leaders in both chambers weighed in with observations – largely general – on what a tax reform package should look like, and in the process revealed some of the issues on which GOP consensus remains elusive.

McConnell: 'I don't think this is going to be 1986'

In the wake of the Senate's recent failure to move Republican-only health care legislation, the chamber's Democrats on August 1 sent to President Trump, Majority Leader McConnell, and Finance Committee Chairman Orrin Hatch, R-Utah, a letter making a pitch for a bipartisan approach to tax reform this year.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170804_1suppA.pdf

In the letter, spearheaded by Minority Leader – and longtime Finance Committee member – Charles Schumer of New York and Finance Committee ranking member Ron Wyden, D-Ore., 43 Democrats and two Independents who caucus with the party urged McConnell and his Republican colleagues not to use the budget reconciliation process to pass tax reform legislation with only Republican support. They said they would be willing to work across the aisle on a bill if it would not cut taxes on the top 1 percent of taxpayers or add to the federal budget deficit.

"Tax reform cannot be a cover story for delivering tax cuts to the wealthiest," the letter stated, adding that Senate Democrats "will not support any effort to pass deficit-financed tax cuts, which would endanger critical programs like Medicare, Medicaid, Social Security, and other public investments in the future."

McConnell quickly dismissed the notion of a unified bill, saying that the conditions set by Democrats for their cooperation would run contrary to the Republicans' vision of rate-reducing tax reform that fuels economic growth.

"We will need to use reconciliation, because we have been informed by a majority of Democrats…that most of the principles that would get the country growing again they're not interested in addressing," McConnell told reporters August 1. "I don't think this is going to be 1986, when you had a bipartisan effort to scrub the code."

Hatch plans post-recess hearings, mark-up: Finance Committee Chairman Hatch told reporters the same day that he plans to take tax reform legislation through a traditional committee process this fall, including hearings and a mark-up, but said Republicans may still have to use reconciliation for passage of a bill because Democrats are obstructing the legislative agenda this year.

"It's their best opportunity to work with us and get something done," he said. "If not, then blame the Democrats."

In comments to reporters on August 3, Hatch reiterated his commitment to holding multiple tax reform hearings on tax reform and a single mark-up of tax reform legislation after the Senate returns to Washington following the summer recess, although he did not announce specific dates.

Could vulnerable Dems cross the aisle?: The three Democrats who did not join their colleagues on the August 1 letter were Sens. Joe Donnelly of Indiana, Heidi Heitkamp of North Dakota, and Joe Manchin of West Virginia. All are up for reelection in 2018 in states carried by President Trump.

McConnell appeared to be eyeing the three as potential crossover votes for a GOP tax reform plan when he told reporters that "there may be a few [Democrats] who may be open to pro-growth tax reform. Even though you do the reconciliation process, nothing prevents any Democrat from supporting it who chooses to."

'Aggressive' timetable

Also this week, White House Legislative Director Marc Short on July 31 laid out an "aggressive" timetable for action on tax reform with legislative mark-ups in the House Ways and Means Committee and Senate Finance Committee in September, followed by House passage in October, Senate passage in November, and a White House signing ceremony before year-end.

"I think we're in for a long fall, legislative calendar-wise," Short said at an event co-sponsored by sponsored by Americans for Prosperity (AFP) and Freedom Partners.

That appears to be consistent with the view of the so-called "Big Six" GOP negotiators from the Senate, House, and the Trump administration, who recently released their consensus principles for tax reform and handed off the work of drafting unified legislation to the two congressional taxwriting committees with the hope that a bill would be on the president's desk by the end of this year. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 27, July 27, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170727_1.html

Few policy specifics

Despite the talk of imminent action, however, administration officials and congressional GOP leaders who discussed tax reform in media interviews and at various public events this week offered few concrete details on key elements of the plan they hope to see enacted into law, although their comments in some cases pointed to potential fissures within the party on certain issues.

Border-adjustment tax alternatives: The GOP consensus statement on tax reform released on July 27 officially laid to rest efforts by Ways and Means Committee Chairman Kevin Brady, R-Texas, and Speaker Paul Ryan, R-Wis., to offset the cost of a corporate rate cut by enacting a border-adjustment tax that generally would eliminate US tax on products, services, and intangibles exported abroad and impose a 20 percent US tax on products, services, and intangibles imported into the US.

In separate interviews on Fox News' *Sunday Morning Futures* with Maria Bartiromo July 30, Brady and Ryan defended the proposal as sound tax policy but said they agreed to abandon it in the interest of moving forward with a tax reform plan that could unite congressional Republicans and members of the Trump administration. But when asked how he intends to replace the revenue – unofficially estimated at over $1 trillion – that the border-adjustment tax was expected to generate, Brady said only that he is working with Senate Finance Committee Republicans and the Trump administration to identify and target for elimination current-law provisions "that really distort the tax code" and lead businesses to make decisions based on tax-motivated rather than economic reasons.

Corporate rate: Marc Short indicated at the AFP-Freedom Partners event that President Trump continues to push for the 15 percent corporate rate that the administration proposed as part of the tax reform principles it released in April.

Brady, meanwhile, told Maria Bartiromo that he intends to get the corporate rate "as low as it can go." He declined to cite a specific rate target, although in response to a question from Bartiromo he indicated that in his view a 28 percent rate would be too high. (The House GOP tax reform blueprint calls for a top corporate rate of 25 percent.)

For his part, North Carolina Republican Rep. Mark Meadows, who chairs the 30-plus member House Freedom Caucus, appeared to align himself with the administration's position.

"You know, some are suggesting a corporate rate of 25, 24 percent. Some go even as low as 20 percent. The president's at 15 percent. I think that something with a one in front of it – whether it's 15 or 17 or 18 – that's where we need to be…and when we do that we will see the economy revive again," Meadows said in remarks delivered at another AFP-Freedom Partners tax reform event in Washington, this one on August 2.

In the Senate, meanwhile, Finance Committee Chairman Orrin Hatch this week appeared to question the feasibility of a significant reduction in the corporate rate.

"[I]t would be kind of miraculous if we could get it down to 25 percent," he told Reuters July 31. "I'd like to get it down to around 20 percent. I'd love to get it at 15 percent if we could. But I think the odds are, we're going to be lucky to get it down at all," he said.

Passthrough issues: Brady told Bartiromo that passthrough businesses, which are currently taxed on the individual side of the code, would see a "dramatically lower rate" under tax reform – although he did not indicate what that rate would be. (The House Republican blueprint calls for a passthrough rate of 25 percent, while the Trump administration backs a rate of 15 percent.)

Brady also touched on the need for anti-abuse rules as part of a new passthrough regime; but he did not provide further details other than to say that House and Senate negotiators are working with the White House and are "getting closer to a good, sustainable way" to differentiate between wages and business income.

Cost recovery: Short told reporters July 31 that the administration will "probably not" back a provision in the House GOP tax reform blueprint that calls for 100 percent first-year expensing for tangible and intangible assets.

The GOP consensus statement calls for "unprecedented capital expensing" for businesses, although it avoids the specific language of the House Republican blueprint. Brady likewise stopped short of advocating for the blueprint proposal during his July 30 Fox News interview. He explained to Bartiromo that the term "unprecedented expensing" in the consensus statement means "the status quo is not good enough," and noted that tax code needs to encourage business investment since that's what drives productivity and higher wages. But he did not address the extent of any possible changes to the expensing rules, nor did he discuss the notion of repealing the net interest expense deduction as a potential tradeoff for liberalized expensing rules. (The blueprint specifically pairs those two provisions, but 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.)

Individual rates: Both Speaker Ryan and Ways and Means Chairman Brady rejected a proposal floated by White House advisor Steve Bannon for a 44 percent top rate on individuals earning over $5 million.

Brady told Maria Bartiromo that “we’re headed downward on tax rates at every level” and that he had no intention of bringing such a proposal before the Ways and Means Committee. Ryan likewise indicated that the House is working toward a rate structure similar to what has been proposed in the Trump administration’s tax reform principles (three brackets of 10, 25, and 35 percent).

Permanence, revenue neutrality: Brady and Ryan both expressed the importance of permanent reforms during their Fox News interviews. Ryan also noted that revenue neutral tax reform is possible under dynamic scoring rules, which take into account certain macroeconomic feedback effects of tax and spending legislation.

In a private meeting with conservative interest groups on July 28, Ryan reportedly stated that he wants to make as many provisions permanent as possible but noted that some – unspecified – provisions may need to be temporary to ensure that an eventual tax reform package complies with budget reconciliation rules, which preclude legislation that increases the federal deficit outside the 10-year budget window.

But House Freedom Caucus Chairman Mark Meadows downplayed the leadership’s emphasis on revenue neutrality in his comments at the August 2 AFP-Freedom Partners tax reform event.

“When we talk about revenue neutral, what that means is we’re going to cut your taxes in one place and we’re going to add them somewhere else. There’s no benefit from that,” he said.

Meadows also expressed support for extending the budget window beyond 10 years for purposes of the yet-to-be-finalized rule instructing Congress to pursue tax reform legislation under reconciliation protections – an idea that has the backing of some conservative congressional Republicans but has run into opposition from Ways and Means Chairman Brady and Speaker Ryan.

PPACA taxes: The Senate stalemate over legislation to repeal and replace the Patient Protection and Affordable Care Act (PPACA) and the decision by that chamber’s Republican leaders to set aside that effort for the time being prompted Brady to tell reporters on July 28 that he does not intend to incorporate repeal of the PPACA’s taxes on businesses and upper-income individuals into a tax reform package.

“We can’t afford to import those into tax reform because the result would be higher tax rates for families and local businesses,” Brady said. He added that, as a practical matter, addressing the PPACA taxes as part of tax reform would likely kill the bill in the Senate.

“They can’t pass the Senate now. What makes you think they could pass the Senate later?” he said.

Recess orders: Sell, sell, sell…

Congressional Republicans have been tasked with selling the public on the need for comprehensive tax reform as they return to their districts and home states for the August recess. (The House adjourned July 28 and the Senate went out of session on August 3. Both chambers will reconvene on September 5.) To that end, House GOP leaders launched a 31 Reasons for Tax Reform e-mail campaign which will run throughout August, with daily messages highlighting ways in which “today’s broken tax code hurts American families, Main Street job creators, and our economy.”
URL: https://waysandmeans.house.gov/31reasons/

President Trump is also expected to play a leading role in promoting tax reform at a series of public events across the country this month.

Crowded fall agenda may impact tax reform timeline

But the aggressive timetables for action on tax reform laid out by negotiators this week could be set back by what is already a very crowded fall legislative agenda. As soon as lawmakers return from recess after Labor Day, they will be confronted by looming deadlines on multiple issues, including government funding, the debt limit, and the pending expiration of a handful of major federal programs. Republicans in the House and Senate will also have to reach an agreement on a new budget resolution for fiscal year 2018 if they intend to move tax reform under the fast-track budget reconciliation process.

Fiscal 2018 appropriations: With respect to government funding, in order to avoid a shutdown on October 1 when fiscal year 2018 begins, Democrats and Republicans will have to arrive at some type of mutual accord on appropriations levels for defense and nondefense accounts. Complicating matters is the so-called “sequester” – statutory caps on all discretionary spending put in place in 2011 as part of a deal to raise the debt limit – which is set to return in full force on October 1.

Two bipartisan deals in recent years have lifted the sequester caps for fiscal years 2014 through 2017 in exchange for savings generated elsewhere in the budget. Many observers believe another such agreement is likely to be required this year in order to garner sufficient Democratic support to move appropriations legislation through the Senate. However, negotiations on such a plan have yet to begin in earnest, which has led to speculation that a stop-gap spending measure – or “continuing resolution” – of some duration may be needed to keep the government open past September 30. (Any such delay in final decision-making on government funding could prove distracting to lawmakers as they try to also make inroads on tax legislation.)

Debt limit: According to a July 28 letter from Treasury Secretary Steven Mnuchin to congressional leaders, Congress also must act by September 29 to lift the statutory debt limit. (A previously enacted debt limit “suspension period” technically lapsed on March 15, 2017; but since that time Treasury has been employing various accounting maneuvers – so-called “extraordinary measures” – to keep the government from breaching the current limit.)
URL: https://www.treasury.gov/initiatives/Documents/Mnuchin%20to%20Ryan%20on%20DISP%20-%207-28-17%20(2).pdf

Mnuchin has been urging Congress to pass a so-called “clean” increase in the debt limit – that is, one free of other legislative policies. Office of Management and Budget Director Mick Mulvaney told reporters August 3 that the White House backs that approach, although it is unclear whether it will appeal to many conservative Republican lawmakers, who in recent years have pushed for spending reductions and budget process reforms in conjunction with any debt limit increase. But any such collateral policies would likely be opposed by congressional Democrats – whose support will be needed to raise the debt limit – which is creating uncertainty as to how this issue will be resolved.

Reauthorizations: Upon its return, Congress will also have to quickly act to reauthorize several federal programs set to expire on September 30, including the Federal Aviation Administration, the National Flood Insurance Program, and the Children’s Health Insurance Program.

Don’t forget about the budget: On top of all this, congressional Republicans will also have to adopt a fiscal year 2018 budget resolution if, as Sen. McConnell intimated this week, they intend to use the budget reconciliation process to fast-track a tax reform bill this fall.

During July, the House Budget Committee approved a fiscal 2018 blueprint that included reconciliation instructions targeted at moving revenue-neutral tax reform alongside $203 billion in spending cuts on entitlement programs; but that plan – which Speaker Ryan has said will come before the full House this fall – faces an uncertain future as moderate and conservative Republicans appear divided over the size and scope of the mandated spending cuts. (For more on the House budget plan, see *Tax News & Views*, Vol. 18, No. 26, July 21, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170721_1.html

Also complicating matters is the fact that House Freedom Caucus Chairman Mark Meadows has stated that the conservative Republicans in his caucus may be reluctant to support the legislative vehicle authorizing an expedited process for tax reform until House leadership provides more details on just what their proposed tax reform plan will include.

“We need more specifics in terms of where we are with tax reform. I’m hopeful that we’ll get those over this August recess,” he told reporters August 2.

And yet another wrinkle was added this week when House Budget Committee Chairman Diane Black, R-Tenn. – who has been working to round up votes for blueprint – announced her candidacy for governor of Tennessee, a step that may require her to relinquish her Budget gavel.

Across the Capitol, Senate Budget Committee Chairman Mike Enzi, R-Wyo., has indicated that his panel will mark up its own budget plan in September.

— Alex Brosseau, Michael DeHoff, and Storme Sixeas
Tax Policy Group
Deloitte Tax LLP

Kautter confirmed for tax policy slot at Treasury

The Senate on August 3 confirmed David Kautter to serve as assistant secretary for tax policy at the Treasury Department by unanimous voice vote.

Kautter most recently headed the Washington National Tax practice for RSM US LLP. He has previously served as the managing director of the Kogod Tax Center and executive-in-residence at the Kogod School of Business at American University and as a partner at Ernst and Young.

In his new position at the Treasury Department, Kautter is expected to play a key role in the ongoing discussions around Republicans' tax reform plans this year. He told Senate Finance Committee members during a July 18 hearing to consider his nomination that he believes "everything should be on the table" as lawmakers seek to revamp the tax code, but he did show some signs of potential dissention from the White House around a few specific tax provisions. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 26, July 21, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170721_3.html

— Michael DeHoff
Tax Policy Group
Deloitte Tax LLP

A note on our publication schedule

Congress has adjourned for the summer recess and both chambers are scheduled to be back in session on September 5. Barring unexpected developments on the tax policy front, Tax News & Views will resume its regular publication schedule when lawmakers return to Washington after Labor Day.

— Jon Traub
Managing Principal, Tax Policy
Deloitte Tax LLP