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Tax reform messaging wars continue following release of 'Big Six' framework

In the wake of releasing their "unified framework" for tax reform on September 27, congressional Republicans and White House officials spent the second half of this week working to rally support for – and, in some cases, defend – the concepts they hope to turn into legislation and send to the president before the end of the year. Meanwhile, many Democrats went on the offensive, decrying the plan as a gift for wealthy taxpayers and big businesses but harmful to the middle-class it purports to help. (For details on the provisions in the GOP tax reform framework, see *Tax News & Views*, Vol. 18, No. 33, Sept. 27, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170927_1.html

Familiar partisan split

It is a debate that is emblematic of the philosophical differences between the two parties. Republicans are touting their tax reform outline as one that will spur economic growth and job creation, lower taxes for most Americans, and make businesses more competitive internationally. Democrats counter that affluent taxpayers would benefit from proposals to eliminate current taxes such as the alternative minimum tax and the estate tax and lower the tax rates for corporations and passthrough entities; but for middle-class taxpayers the potential benefits stemming from an increased standard deduction would be blunted by the framework's proposal to eliminate the personal exemption.

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With many key details – including the income cutoffs for the new proposed rate brackets and many of the revenue offsets to pay for rate cuts and other tax relief – still to be filled in during the legislative drafting process, it is impossible to determine exactly how the proposals in the framework will affect taxpayers at various income levels. For now, this leaves the playing field open for dueling messages.

Many Democrats – including Senate Finance Committee ranking member Ron Wyden of Oregon – issued scathing remarks about the framework; but others – including Senate Democratic Leader Charles Schumer of New York and House Ways and Means Committee ranking member Richard Neal of Massachusetts – expressed support for tax reform generally but took issue with the Republicans' proposal and said they hope to help shape the legislation.

Cohn stands firm on business rates: At a press briefing on September 28, however, White House Economic Director Gary Cohn left little room for Democratic input – at least on the issue of business tax rates.

"Our opening offer and our final offer are on the table," Cohn said of the framework. "We were happy to start at [a] 25 [percent rate for passthrough entities] and we're happy to go lower, and we're happy to start at 20 [percent] on corporate and go lower. So there's our opening offer. If [Schumer] wants to counter [with] something lower, we're very negotiable."

Cohn was one of the members of the "Big Six" tax reform negotiating team, along with Treasury Secretary Steven Mnuchin, House Speaker Paul Ryan, R-Wis., Senate Majority Leader Mitch McConnell, R-Ky., House Ways and Means Committee Chairman Kevin Brady, R-Texas, and Senate Finance Committee Chairman Orrin Hatch, R-Utah.

Hatch hints at wiggle room on state-and-local tax deduction: Finance Chairman Hatch, meanwhile, suggested that there could be some flexibility when it comes to the future of the individual deduction for state and local taxes.

"If we can keep it, I'd like to keep it," Hatch told reporters September 28.

Although the framework does not explicitly call for eliminating the deduction to help offset the cost of lower rates, members of the Big Six have commented publicly in recent weeks that the provision is a target for repeal as part of tax reform – a prospect that has raised concern among lawmakers in both parties who represent constituents in high-tax jurisdictions.

Trump puts the squeeze on vulnerable Dems

President Trump, for his part, continued his efforts to win support for the GOP tax reform plan from Democratic senators up for re-election next year in deep red states.

"If Sen. [Joe] Donnelly doesn't approve it – because, you know, he's on the other side – we will come here, we will campaign against him like you wouldn't believe," the president said September 27 during a tax-focused speech in Donnelly's home state of Indiana.

"I think they're gonna approve it," Trump said of the GOP tax reform plan. "Actually, I think we'll have numerous Democrats come across because it's the right thing to do."

Trump has put similar pressure on Sens. Heidi Heitkamp of North Dakota, Claire McCaskill of Missouri, and Joe Manchin of West Virginia during recent appearances in their states and at White House meetings. He is likewise expected to target other red-state Senate Democrats when he speaks at tax reform events in the coming weeks.

Brady seeks business involvement

In a speech at the US Chamber of Commerce on September 28 – one of several appearances he made following the rollout of the framework – House Ways and Means Chairman Brady opened the door for the business community's continued involvement in the tax reform process as he addressed the technical work the taxwriting committees must now do to turn the framework into a bill, including the rules for transitioning from the current system to a new one.

"We want to move from this old clunker of a tax car that cannot compete around the world to a new model that frankly can keep up [with] or exceed any of the newer models on the road today around the world. And that transition to that new car matters," Brady said. As House taxwriters develop comprehensive legislation, they will be "reaching

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out to have industry test drive some of these provisions and the transition rules" to ensure that they "are getting the technical drafting of this right," he added.

Finance Committee schedules hearing on international tax reform

In other developments this week, the Senate Finance Committee announced that it will hold a hearing on international tax reform issues at 10:00 a.m. on October 3. Witnesses will include Bret Wells, a professor at the University of Houston Law Center; Kimberly Clausing, a professor of economics at Reed College in Portland, Ore.; Stephen E. Shay, a senior lecturer at the Harvard Law School; and Itai Grinberg, a professor at the Georgetown University Law Center.

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Combined hurricane tax relief-FAA extension package clears Congress, heads to White House

The House and Senate this week approved and sent to President Trump legislation that combines tax relief for victims of three recent hurricanes with an extension of a soon-to-expire authorization for the Federal Aviation Administration (FAA).

The Disaster Tax Relief and Airport and Airway Extension Act of 2017 (H.R. 3823) passed in the House the morning of September 28. The Senate approved the measure later in the day – after stripping out a provision that would have allowed private insurers to participate in the National Flood Insurance Program. House lawmakers cleared the amended bill after it was sent back from the Senate.
URL: https://www.congress.gov/115/bills/hr3823/BILLS-115hr3823ih.pdf

President Trump is expected to quickly sign the measure into law.

Hurricane tax relief

As approved, the bill would provide targeted, temporary tax relief to individuals and businesses affected by Hurricanes, Harvey, Irma, and Maria. The Joint Committee on Taxation staff has estimated that the relief package, which is not offset, would decrease federal revenues by just over $5.6 billion between 2018 and 2027.
URL: https://www.jct.gov/publications.html?func=startdown&id=5024

Employee retention incentives: The bill would provide a temporary tax credit for 40 percent of wages (up to $6,000 per employee) paid by a disaster-affected employer to an employee from a core disaster area.

The provision would be effective for wages paid or incurred beginning August 23, 2017 (for employers affected by Hurricane Harvey); September 4, 2017 (for employers affected by Hurricane Irma); or September 16, 2017 (for employers affected by Hurricane Maria). The credit would be available through January 1, 2018, for all affected employers.

Access to retirement funds: The measure would make it easier for hurricane victims to gain emergency access to funds in qualified retirement plans by:

- Waiving the 10 percent early withdrawal penalty for qualified hurricane-relief distributions and allowing income tax on the distributions to be paid over three years;
- Permitting recontribution of retirement plan withdrawals for home purchases that were cancelled due to eligible disasters; and
- Relaxing the rules for loans from retirement plans for qualified hurricane relief.

These provisions would be effective upon enactment.

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Deduction for personal casualty losses: For individuals who incur uncompensated disaster-related losses, the bill would temporarily eliminate the current-law requirements that personal casualty losses must exceed 10 percent of adjusted gross income to qualify for deduction. The measure also would allow nonitemizers with qualifying disaster-related losses to take advantage of this tax relief.

These provisions would apply to losses arising on or after August 23, 2017 (for losses related to Hurricane Harvey); September 4, 2017 (for losses related to Hurricane Irma); or September 16, 2017 (for losses related to Hurricane Maria).

Earned Income Tax Credit and Child Tax Credit: The bill would allow taxpayers to determine their Earned Income Tax Credit and Child Tax Credit for 2017 based on their earned income from the immediately preceding year (effective for taxable years beginning after January 1, 2016).

Charitable giving: For businesses and individuals, the bill would temporarily suspend limitations on the deduction for charitable contributions associated with qualified hurricane relief (effective for contributions made during the period beginning on August 23, 2017, and ending on December 31, 2017).

FAA authorization

The bill would reauthorize the FAA – including fuel and passenger excise taxes that provide the agency's dedicated revenue stream – through March of 2018. The FAA's current authorization is set to expire September 30.

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Senate scraps floor vote on Graham-Cassidy PPACA repeal measure

Senate Republican leaders announced September 26 that they would not hold a floor vote on legislation sponsored by Sen. Lindsey Graham, R-S.C., and Finance Committee member Bill Cassidy, R-La., that would dismantle major portions of the Patient Protection and Affordable Care Act of 2010 (PPACA) but retain most of the PPACA's revenue-raising tax provisions after it became clear that the measure would not attract enough GOP votes to ensure passage.

The decision brings to a close a last-ditch effort to move a health care reform bill through the chamber while it still enjoys fast-track budget reconciliation protections included in the soon-to-expire budget resolution for fiscal year 2017.

The Graham-Cassidy bill (H.R. 1628) was formally introduced on September 13 as a Senate substitute amendment to PPACA repeal legislation that was narrowly approved by the House of Representatives in May. (For prior coverage of the House bill, see *Tax News & Views*, Vol. 18, No. 16, May 5, 2017.) Graham and Cassidy developed their proposal after attempts to move several different iterations of PPACA repeal-and-replacement legislation in the Senate during July were unsuccessful. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 28, July 28, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170505_1.html
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170728_1.html

In very broad terms, the bill would dismantle the overall structure of the PPACA (including the expansion of the Medicaid program, tax credits to help lower-income individuals afford the cost of health insurance coverage, and cost-sharing reduction subsidies) in 2020, and replace it with block grants for states to use to administer their own respective health insurance plans.

On the revenue side, the bill would effectively repeal the PPACA's individual and employer mandates by reducing the penalties for noncompliance to zero retroactive to calendar year 2016, and would repeal outright the medical device excise tax effective for sales after December 31, 2017. But it would retain most of the other tax offsets that currently fund the PPACA, such as the 3.8 percent net investment income tax and the 0.9 percent Medicare Hospital Insurance tax assessed on certain upper-income individuals, as well as corporate offsets such as the annual fee on health

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insurance providers, the fee on branded drug importers, limits on executive compensation for certain employees of covered insurance providers, and the excise tax on "Cadillac" group health insurance programs.

Too little time, too many defections

Senate GOP leaders had hoped to hold a vote on the measure while budget reconciliation protections that permit passage by a simple majority vote still apply. (The Senate parliamentarian recently held that the fast-track budget reconciliation protections for PPACA repeal-and-replacement legislation expire on September 30, along with the fiscal year 2017 budget resolution that included the reconciliation instruction authorizing the legislation. Without the reconciliation protections, the legislation would have to move under regular order and would be subject to the 60-vote threshold normally required to overcome procedural hurdles in that chamber.)

With Republicans holding 52 seats in the Senate, and the chamber's 46 Democrats plus the 2 Independents who caucus with them expected to vote in lockstep against the measure, the GOP could afford only 2 defections and still scrape together the 50 votes they needed to get the Graham-Cassidy bill across the finish line. (Vice President Mike Pence would have supplied fifty-first vote in the case of a tie.)

Although the bill appeared to gain momentum within the Republican conference since its introduction, it stumbled badly in recent days after three Republicans – Sens. Rand Paul of Kentucky, John McCain of Arizona, and Susan Collins of Maine – declared themselves irrevocably in opposition. (Paul felt the bill retains too many elements of the PPACA; McCain argued that a significant change to the nation's health care structure should move under regular order with bipartisan participation; and Collins objected to the measure's proposed cuts to Medicaid.) The three GOP holdouts guaranteed that the legislation would fail if it went to the Senate floor.

Further action on hold

Majority Leader Mitch McConnell, R-Ky., told reporters September 26 that although Senate Republicans remain committed to repealing the PPACA, the chamber will turn its immediate attention to tax reform.

"We have not given up on changing the American health care system. We're not going to be able to do that this week. But it is still out ahead of us and we have not given up on that," McConnell said. "We do think it is time to turn to our twin priority, reforming the tax code. We have reached significant agreements to go forward. I am optimistic that we will achieve that," he continued.

Vice President Pence reportedly told Senate Republicans at their September 26 conference lunch that lawmakers should address PPACA repeal before the 115th Congress adjourns at the end of 2018.

Some Senate Republicans suggested adding a reconciliation instruction in the yet-to-be-adopted fiscal year 2018 budget resolution that would allow Congress to pursue health care reform and tax reform under reconciliation protections – an idea that GOP leaders dismissed as too difficult both procedurally and politically. Across the Capitol, House Freedom Caucus Chairman Mark Meadows, R-N.C., told reporters that he would not support a unified budget resolution that packaged tax reform along with PPACA repeal. (The Freedom Caucus includes roughly three dozen ultraconservative Republicans, enough to block House passage of any legislation it finds objectionable, assuming there is also unified Democratic opposition.)

Graham, who has said that he and Cassidy would like to continue refining their proposal, told reporters that congressional Republicans may take up the issue again in 2018 but indicated that lawmakers would try to include a reconciliation instruction for health care reform in a budget resolution for fiscal year 2019.

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GOP corporate tax reform proposals hold state tax implications

The federal corporate tax reform proposals included in the "unified framework" released by the "Big Six" negotiating team of congressional Republican leaders and White House officials September 27 present the potential for sweeping change for state corporate income taxes that taxpayers should bear in mind as lawmakers begin the process of transforming a set of policy aspirations into detailed legislative proposals. (For details on the framework, see *Tax News & Views*, Vol. 18, No. 33, Sept. 27, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170927_1.html

Conform or decouple?

It is reasonable to expect each state to respond to federal tax reform based on its unique budget issues and political constituencies. Most states have either rolling or fixed-date conformity to the Internal Revenue Code or use federal taxable income as the starting point for calculating state taxable income. However, unlike the federal government, the states both cannot engage in deficit spending and have the ability to legislate changes relatively quickly. Accordingly, state legislatures will need to evaluate whether they can afford to conform to or should decouple from revenue-decreasing proposals such as immediate expensing.

Territoriality, minimum taxes, and deemed repatriation

The revenue-raising proposals in the framework raise complex state issues as well. For example, the framework proposes to shift from a worldwide to a territorial system for taxing foreign-source income of US multinationals, accompanied by base-erosion protections in the form of a current minimum tax (at a reduced rate) on foreign profits. The prospect of current taxation of foreign profits could prompt states to reconsider their separate, water's edge combined (or water's edge combined plus "tax havens") filing methods.

Further, as part of the transition to a territorial system, the framework proposes that overseas earnings would be subject to a one-time deemed repatriation tax (at an unspecified rate and payable over an unspecified period). While states will presumably want to tax their share of the deemed repatriation of accrued foreign profits, separate-filing states and states with filing groups that differ from the federal filing group may find themselves unable to do so under existing law. Accordingly, we expect the state response to federal tax reform to vary from state to state, creating a corresponding level of complexity for taxpayers to address.

State-and-local-tax deduction

Although the framework does not explicitly address this issue, members of the Big Six have stated in public comments that tax reform should raise revenue by eliminating the deduction for state and local taxes paid. Eliminating the deduction would have the most direct impact on state and local governments by effectively making state and local taxes more expensive for millions of individuals. This proposal – which would generate significant federal revenue, primarily from taxpayers in high-tax states – has generated, and will likely continue to generate, opposition from certain state officials and promises to be among the more controversial elements of the tax reform debate.

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