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Senate GOP clears budget plan aimed at fast-tracking tax reform; House may follow suit in short order

Even as President Trump made overtures this week to Senate Finance Committee Democrats on bipartisan tax reform, Senate Republicans successfully cleared a fiscal year 2018 budget resolution October 19 that has as its primary focus the consideration of a subsequent tax reform bill on a filibuster-proof basis that could, on net, increase deficits over the next decade by as much as $1.5 trillion.

During its consideration of the plan, the Senate GOP adopted certain (relatively minor) House-desired changes; as a result, a conference committee may not be necessary and the House could pass the revised budget in the coming days.

The details

The budget resolution cleared the Senate on an almost straight party-line vote of 51-49. The budget was opposed by all Senate Democrats, as well as Sen. Rand Paul, R-Ky., who objected to several of the nontax aspects of the plan, including its call for fiscal 2018 defense appropriations above the levels allowed under the current statutory caps on discretionary spending (*i.e.*, the "sequester") and the fact that the overall plan would not achieve balance within the 10-year budget window.

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The broad strokes of the Senate plan include roughly $4.9 trillion of spending cuts – mainly coming from unspecified reductions in mandatory spending programs and to a lesser extent from nondefense appropriations and reduced debt service costs on account of the plan's deficit reduction. The blueprint also banks roughly $1.4 trillion of assumed savings from added economic growth. (For more detail on the Senate budget, including what it says, or does not say, about dynamic scoring and adjusting the revenue baseline for tax reform, see *Tax News & Views*, Vol. 18, No. 35, Oct. 6, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/171006_1.html

'Reconciliation' and the Corker-Toomey deal: At the budget's core – and a main reason Republicans were able to successfully band together to advance the plan – is the inclusion of so-called "budget reconciliation" instructions targeted at advancing subsequent tax legislation on a filibuster-proof basis in the Senate. (Provided strict parliamentary and procedural rules are met, legislation moved under budget reconciliation can pass the House and Senate with simple majority votes, making it a powerful tool for Republicans who control 52 Senate seats, short of the three-fifths majority – that is, 60 votes – normally needed to advance legislation under regular order in that chamber.)

The vision of reconciliation included in the Senate budget calls on the taxwriting Finance Committee to report legislation that increases the deficit by no more than $1.5 trillion over the next decade – which mirrors a handshake deal struck last month between Senate Budget Committee Republicans Bob Corker of Tennessee and Pat Toomey of Pennsylvania. (Although a budget resolution cannot stipulate specific policies to be reported by other committees, it has been widely telegraphed that the Senate instruction currently in play is targeted at moving a tax reform bill.)

Tax-related amendments offered – some adopted, many swatted away: A number of tax-related amendments were voted on both during debate on the budget resolution, as well as during the so-called "vote-a-rama" – or the period after a budget's set 50-hour debate time has lapsed and an unlimited number of amendments can be offered and voted on *without* debate.

In many cases, these amendments were structured as so-called "reserve funds" which in theory are designed to shield subsequent conforming legislation from parliamentary points of order related to the budget, but in practical terms are usually intended mainly for political messaging (that is, to show support, or lack thereof, for a broadly stated policy).

Among the amendments that received votes were proposals to:

- Restore proposed Medicaid cuts and reduce tax breaks for the wealthy (offered by Senate Budget Committee ranking member Bernie Sanders, I-Vt., and voted down 47-51; a separate Sanders amendment to block tax cuts for the top 1 percent was ruled out-of-order);
- Restore proposed Medicare cuts and close special-interest tax loopholes (offered by Finance Committee member Bill Nelson, D-Fla., and voted down 47-51);
- Direct tax relief at families with children (offered by Finance Committee member Dean Heller, R-Nev., and approved 98-0);
- Direct tax relief at small businesses along with rules to "prevent upper-income taxpayers from sheltering income from taxation at the appropriate rate" (offered by Sen. Susan Collins, R-Maine, and agreed to by voice vote);
- Reduce federal deductions "such as the state and local tax deduction which disproportionally [sic] favors high-income individuals" in order to ensure relief for middle-income households (offered by Sen. Shelley Moore Capito, R-W.Va., and agreed to 52-47);
- Strike the budget's exemption for tax reform from the Senate's Pay-As-You-Go rule (offered by Finance Committee member Mark Warner, D-Va., and voted down 47-51); and
- Strike the reconciliation instructions related to tax reform (offered by Finance Committee ranking member Ron Wyden, D-Ore., and voted down 47-52).

On to conference committee? Likely not

Given the House had cleared its fiscal 2018 budget resolution on October 5 (for prior coverage, see *Tax News & Views*, Vol. 18, No. 35, Oct. 6, 2017), a key question as the Senate proceeded to pass its plan had been whether the two chambers would establish a formal conference committee to reconcile their respective plans, or whether the House would instead simply take up and attempt to pass the Senate plan. The latter approach would be borne mainly of a desire to start the legislative process on tax reform before a crush of other deadlines takes center stage – including a December 8 government funding deadline and a likely winter or spring 2018 deadline to raise the debt limit (both of

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which will require 60 votes in the Senate), as well as encroaching primary elections which are set to begin in March of next year.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/171006_1.html

One might have assumed a conference committee was in the offing given the stark differences between the two budgets, especially those related to the fiscal impact of tax reform and the House budget's much broader set of reconciliation instructions. The House budget instructs 11 committees to report $203 billion in deficit-cutting legislation that would move alongside *revenue-neutral* tax reform. The Senate budget, meanwhile, includes just one other instruction for the Energy and Natural Resources Committee to report legislation that cuts the deficit by at least $1 billion, ostensibly aimed at expanding oil production in the Arctic National Wildlife Refuge (ANWR).

But the odds of House and Senate leaders convening a formal conference committee dwindled markedly on the evening of October 19 when – shortly before Senate consideration came to a close – Senate Budget Committee Chairman Mike Enzi, R-Wyo., offered, and the Senate adopted, a handful of changes desired by House GOP leaders related to fiscal year 2018 defense appropriations, the process by which a tax reconciliation bill will wind through the House (*i.e.*, it may go straight from the Ways and Means Committee to the House floor, rather than stopping over at the House Budget Committee), and other matters, while leaving in place the Senate's vision of reconciliation aimed predominantly at a net $1.5 trillion tax cut devoid of concurrent spending cuts.

Taken together – and assuming the acquiescence of the vast majority of rank-and-file House Republicans – it currently appears these changes may be sufficient to avoid a conference committee and the House GOP could clear the Senate-passed plan as soon as the week of October 23.

Even before the full Senate ended debate on its budget plan, two clues indicated GOP leaders may have been hoping the House would simply take up the Senate-passed budget. First, Senate Budget Committee Chairman Enzi offered the budget bill his committee reported to the full Senate on October 5 (S. Con. Res. 25) as a substitute amendment to the House-passed budget (H. Con Res. 71). Thus, as a procedural matter, the budget that passed the Senate technically remains the House legislative vehicle, but with replacement language.

Second, the Senate budget – ever since it was publicly released on September 29 – included reconciliation instructions not only to Senate Finance and Energy and Natural Resources Committees, but also to the relevant House committees with jurisdiction over the envisioned policies to be reconciled – in this case, the Ways and Means Committee for tax reform and the Committee on Natural Resources for ANWR-related policy. Typically, a budget resolution – prior to a conference committee between the two chambers – only includes reconciliation instructions (if any) to committees within the chamber in which the budget is being considered.

House developments: GOP taxwriters to nail down tax reform details

House Ways and Means Committee Chairman Kevin Brady, R-Texas, has indicated that he will release the text of a comprehensive tax reform bill shortly after a unified budget resolution is approved in the House and Senate, with a formal committee mark-up to follow. In preparation for that phase of the tax reform process, Ways and Means Committee Republicans will gather for two multi-hour meetings on October 24 and 25, a committee spokesperson announced this week. The two dozen taxwriters have been meeting at length in recent weeks to make the policy decisions necessary to flesh out the broad tax reform framework released September 27 by the so-called "Big Six" negotiators from the House, Senate, and administration (namely, Brady, House Speaker Paul Ryan, R-Wis., Senate Finance Committee Chairman Orrin Hatch, R-Utah, Senate Majority Leader Mitch McConnell, R-Ky., Treasury Secretary Steven Mnuchin, and National Economic Council Director Gary Cohn.)
URL: https://waysandmeansforms.house.gov/uploadedfiles/tax_framework.pdf

While Brady and others have kept a close hold on the details that may have been determined so far, there were further hints this week about some of the provisions on which Republicans are focusing, including the treatment of passthrough entities, business interest and expensing, and some individual taxpayer incentives that have long been considered untouchable.

Passthrough issues: The GOP's proposal to shift passthrough business income out of the individual side of the tax code and into a new schedule with a top rate of 25 percent has drawn criticism from Democrats and some tax analysts, who argue that the change will open a loophole for wealthy taxpayers. Sensitive to the charge that "guardrails" will be necessary to prevent the wealthiest passthrough owners from reclassifying wage income as

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business income to take advantage of the gap between the top individual rate and the new passthrough rate, Republicans are working to craft such anti-abuse rules; but it remains unclear whether the anticipated legislation will include detailed guidance or instead leave the specifics to the regulators at the Treasury Department and IRS. Treasury Secretary Mnuchin has previously said that the new rate will not be available to services companies, such as law firms and accounting and investing firms.

Corporate rate: Also under discussion this week was the possibility of a gradual phase-in for the proposed new target corporate tax rate of 20 percent. Taxwriters, including Tax Policy Subcommittee Chairman Peter Roskam, R-Ill., confirmed to reporters that the committee is considering implementing the 20 percent rate over three or five years instead of immediately – an approach similar to the one adopted by then-Ways and Means Chairman Dave Camp in the tax reform proposal he introduced in 2014. This would help lower the cost of the tax bill in the initial years of enactment – something Republicans are focused on as some in the party oppose increasing the federal budget deficit – but would almost certainly be less than appealing for corporations anticipating a significant near-term rate drop.

Brady was noncommittal when asked in an interview with Reuters whether the rate would take effect in the first year, saying only that "[w]e're moving toward that whole design [of a 20 percent corporate rate]."

Business interest expense: At an October 18 event hosted by Rice University's Baker Institute for Public Policy in Houston, Brady reiterated the framework's position that the current-law deduction for business interest expense will be limited in the forthcoming bill. He said the taxwriters' goal is to minimize the current bias in favor of borrowing, making the many financing options that companies have "essentially neutral."

Brady did not elaborate on how "limited" the deduction would be in the forthcoming proposal, but there has been some talk among Republicans about limiting the deduction to net interest up to 30 percent of EBITDA (that is, earnings before interest, tax, depreciation, and amortization – a standard that is used by several other countries, including the United Kingdom).

Mortgage interest, charitable giving deductions: Brady told the audience at Rice University that House taxwriters are "exploring the home mortgage deduction and charitable [giving deduction]" and noted that he and his colleagues are examining ways extend those benefits to non-itemizers.

"Is there a better and fairer way to allocate those resources?" he asked.

On the taxpayer side, the Mortgage Bankers Association (MBA), moving away from a long-held position, signaled in an October 12 letter to the Big Six that its members are open to changes in the deduction taxpayers can claim for mortgage interest payments, a provision that has been considered sacrosanct in tax reform discussions. This comes after the National Association of Homebuilders (NAHB) took a similar stance earlier in the month.

While still supportive of the current deduction, the groups said they will look at related changes in the context of the broader tax reform proposal and are willing to consider alternative incentives for home ownership. The framework's proposed changes, including a doubling of the standard deduction, will "provide policymakers with a tangible opportunity to pursue alternative homeownership tax incentives – and perhaps target those benefits more efficiently to low- to moderate-income borrowers," the MBA said in its letter. (The National Association of Realtors, another longtime opponent of modifications to the mortgage interest deduction, has not changed its stance in opposition to the doubling of the standard deduction.)

Cutting back on SALT?: Discussions also have continued about the controversial proposal to eliminate the current deduction for state and local taxes (SALT) paid by individuals. House Republicans who represent districts where taxpayers disproportionately benefit from the current-law deduction have argued that any reform should limit the deduction rather than repeal it outright so that the benefits flow to middle-income homeowners but not to wealthier individuals.

While taxwriters have consistently said that "everything is on the table" when it comes to reforming the business tax code, to date there has been no public discussion of eliminating the SALT deduction for businesses.

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Senate developments: Hatch ~~bullish~~ bearish about corporate integration prospects

On the other side of the Rotunda, taxwriters generally have been tight-lipped about what might be included in an eventual Senate Finance Committee tax reform package. That seemed to change when Finance Committee Chairman Orrin Hatch told *Politico* early this week that some version of a corporate integration proposal was likely to appear in both the Senate's tax reform bill and the final package that Congress sends to the White House.

But Hatch's outlook was decidedly less optimistic when he addressed the issue with reporters on October 19.

"It's not a given – put it that way," he said.

According to Hatch, "people are interested in" integration but "everybody has different ideas" and he will have to "find the right situation to really push it."

Corporate integration, which seeks to reduce the double taxation on corporate income by exempting dividends paid to shareholders, has been discussed frequently in recent months. Hatch has pitched it as a way to bring the *effective* tax rate for corporations that pay dividends closer to 20 percent in the event that taxwriters drafting a tax reform plan have to settle on a *statutory* rate that's higher than their 20 percent target to ensure that the package complies with budget rules that prohibit legislation moved under fast-track reconciliation protections from increasing the federal deficit outside the 10-year budget window.

The GOP tax reform framework leaves the door open for a corporate integration proposal, noting that the congressional taxwriting committees "may consider methods to reduce the double taxation of corporate earnings." Hatch has been an outspoken advocate of corporate integration and has spent considerable time over the past few years developing a plan that would reportedly couple a dividends-paid deduction with a withholding tax on both interest and dividend payments, although he has not released a formal proposal. (More recently Hatch has been said to be considering a "partial corporate integration" plan that likely would not have a withholding component.) In a recent Finance Committee hearing on international tax reform, Hatch and one witness discussed how the use of integration could reduce disparities in the current-law tax treatment of corporations and passthroughs and the treatment of debt and equity.

One concern over integration has been that so much of corporate stock is held by tax-exempt entities (pension funds, for example) and foreign shareholders that if the income was exempt at the corporate level there would be no way to collect any tax revenue. (A possible solution is to limit the percentage of dividends that can be deducted to mirror the amount of corporate stock held by entities that pay no tax.)

It's worth noting there has been no real discussion of corporate integration in the House, so its inclusion in the Senate version of tax reform legislation would need to survive a conference to wind up in the final package.

Trump reaches out to Finance Committee Dems: In other developments, President Trump continued his efforts to win support for tax reform among Senate Democrats by inviting a select group of Democratic Finance Committee members (along with their Republican colleagues) to join him for lunch at the White House October 18 to discuss bipartisan possibilities for tax reform.

Aside from Finance Committee ranking member Ron Wyden of Oregon, all the Democrats invited hail from states that Trump carried in the 2016 presidential race: Sherrod Brown of Ohio, Bob Casey of Pennsylvania, Claire McCaskill of Missouri, Bill Nelson of Florida, and Debbie Stabenow of Michigan.

Brown commented after the meeting that "[t]here was a lot of talk about bipartisanship, there always is, and I take people at their word."

In fact, Trump asked Wyden and Hatch to create a bipartisan working group for tax reform. But the idea wasn't particularly popular with Republican taxwriters, including Majority Whip John Cornyn of Texas, who said "I don't really personally see the benefit of creating additional structure. I think we've got all the tools we need." (The Finance Committee formed five bipartisan working groups focusing on various aspects of tax reform in 2015. That process culminated in the release of a series of reports with varying degrees of specificity and consensus. For coverage of the working groups' reports, see *Tax News & Views*, Vol. 16, No. 23, July 10, 2015.)
URL: http://newsletters.usdbriefs.com/2015/Tax/TNV/150710_1.html

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Wyden also seemed skeptical of bipartisanship, claiming that Democrats agree on the message behind reform but not on the current approach adopted by the GOP.

"Democrats agree that our tax code is broken, and you fix it with reforms focused on simplicity and putting more dollars in middle class paychecks," he said in an October 18 news release issued after the meeting. "But as of today, the Trump plan would increase taxes on hardworking families while giving away trillions of dollars in tax cuts to the biggest corporations and the ultra-wealthy. You're not going to reach bipartisanship by plowing forward with this con job on the middle class."

Still Hatch commended Democrats for being open to working in a bipartisan manner, although it remains to be seen what that entails. Finance Committee member John Thune, R-S.D., told reporters after the meeting that Democrats may be more flexible on the use of "dynamic" scoring – allowing macroeconomic feedback from reform to be taken into account for revenue scoring purposes – than had previously been expected.

Over the last several weeks, President Trump has also attempted to cajole "red state" Democrats into supporting tax reform during a series of campaign-style rallies in Pennsylvania, Missouri, Indiana, and West Virginia. Additionally, Trump's daughter Ivanka and her husband Jared Kushner hosted several red state Democrats – Claire McCaskill of Missouri, Heidi Heitkamp of North Dakota, and Joe Manchin of West Virginia – to discuss tax reform over dinner at their home on October 16.

View from the administration

President Trump, for his part, broke no new ground on tax policy in remarks he delivered at the Heritage Foundation's annual President's Club meeting in Washington October 17, in which he promised that the GOP tax reform framework would provide a "tax cut for everyday working Americans," reduce the "crushing" corporate tax rate "to restore America's competitive edge," give passthrough business owners "the biggest reduction in taxes in the history of this country," and eliminate "the horrible and very unfair estate tax."

Trump contended that the framework's proposal to move to a territorial system for taxing foreign-source income of US multinationals would result in a massive infusion of cash into the US economy as businesses repatriate assets currently held offshore. He also doubled down on recent claims by his Council of Economic Advisers (CEA) that the combination of the framework's more favorable international tax regime plus the corporate rate cut would redound to the benefit of the middle class, saying that "the typical American household" likely would see "around a $4,000 pay raise." (The CEA laid out the details behind that assertion in a report released October 16.)
URL: https://www.whitehouse.gov/sites/whitehouse.gov/files/documents/Tax%20Reform%20and%20Wages.pdf

Treasury Secretary Steven Mnuchin, meanwhile, stated on the *Politico Money* podcast October 18 that the primary goals of tax reform are creating a middle-income tax cut and a competitive business environment; but he acknowledged that some of the benefits of tax reform will inevitably flow to upper-income individuals.

"The top 20 percent of the people pay 95 percent of the taxes. The top 10 percent pay 81 percent of the taxes. So when you're cutting taxes across the board it's very hard not to give tax cuts to the wealthy [along] with tax cuts for the middle class," he said.

Mnuchin characterized discussion around estate tax repeal as both an "economic" and a "philosophical" issue.

"People pay taxes once. Why should people have to pay taxes again when they die?" he asked.

Mixed signals on timing

In the midst of the back-and-forth over what should or shouldn't be included in a tax reform package, congressional Republican leaders and administration officials have sent mixed signals recently on the question of when a tax code overhaul will be enacted into law.

House Speaker Paul Ryan has set a deadline for enacting tax reform by the end of this year and has said he intends to keep the House in session through Christmas to make that happen. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 36, Oct. 13, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/171013_1.html

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President Trump and Senate Majority Leader Mitch McConnell this week offered a more cautious assessment. In comments to reporters after an October 16 meeting at the White House, the president and the Senate majority leader said they remain intent on enacting tax reform this year; but, invoking the legislative legacies of Ronald Reagan and Barack Obama, they appeared to concede that the process could slip into the second year of the Trump administration.

"I would like to see it be done this year. But don't forget it took years for the Reagan administration to get taxes done. I've been here for nine months," Trump said.

McConnell likewise reminded reporters that "it is important to remember that Obama signed Obamacare in March of year two [and] signed Dodd-Frank in July of year two."

Treasury Secretary Mnuchin, for his part, channeled both Ryan's certainty about action this year and Trump and McConnell's reservations.

During his appearance on the *Politico Money* podcast October 18, Mnuchin offered his "absolute guarantee" that tax reform will be finalized in 2017 and predicted that a conference bill would be on President Trump's desk "by early December." But in an interview on Fox News a day earlier, he commented that although the "objective" is to get a bill to the president by December, wrapping up work this year would be "extraordinary" and there is "no artificial deadline."

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Another House GOP taxwriter headed for the exit

House Ways and Means Committee member Pat Tiberi, R-Ohio, announced October 19 that he will leave Congress before the end of his current term to head up the Ohio Business Roundtable. He did not cite an official departure date but indicated that his resignation will become effective by January 31, 2018.

Tiberi was first elected to the House in 2000 and is the fourth-ranking Republican on the taxwriting panel. He currently chairs the Ways and Means Health Subcommittee and is a former chairman of the panel's Subcommittee on Tax Policy.

Tiberi's announcement is the latest in a series of pending changes to the Ways and Means GOP roster. In the past few months, six other Republican taxwriters have also announced plans to leave Congress, although those lawmakers intend to remain in office until their terms expire at the end of 2018. Three members – Reps. Sam Johnson of Texas, Dave Reichert of Washington, and Lynn Jenkins of Kansas – are retiring; another three – Reps. Diane Black of Tennessee, Jim Renacci of Ohio, and Kristi Noem of South Dakota – are running for governor of their respective home states.

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