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Trump administration unveils fiscal 2020 budget package

Using some assumptions and policy recommendations unlikely to be adopted by the legislative branch, President Donald Trump this week sent to Congress a fiscal year 2020 budget package that envisions declining budget deficits – and eventual balance just beyond the 10-year budget window – even as it assumes a $1.1 trillion extension of provisions in the 2017 tax cut law that are scheduled to sunset after 2025. Treasury Secretary Steven Mnuchin defended the tax-and-spending blueprint during two subsequent hearings with House and Senate taxwriters.

Ambitious fiscal goals...

At a high level, Trump’s budget – released on March 11 – sees deficits peaking at $1.1 trillion in fiscal year 2020 (that is, the upcoming fiscal year that begins on October 1) and then staging a steady descent over the next decade, falling to only $202 billion in fiscal 2029. That 2029 deficit would be just 0.6 percent of gross domestic product (GDP), far below the average deficit of 2.9 percent of GDP registered over the past 50 years.

URL: https://www.whitehouse.gov/omb/budget/
year 2022. By 2029, the publicly held debt, at 71.3 percent of GDP, would be smaller than it is today (at about 79 percent of the economy).

...But with some potentially divisive policies and significant assumptions

But Trump’s blueprint has come in for heavy criticism from some budget watchers and virtually all Democratic lawmakers for its ambitious assumptions about economic growth and for some of its policy recommendations, particularly with respect to the plan’s proposed annual appropriations levels for defense and nondefense accounts and the manner in which it evades the statutory caps (known as the “sequester”) with respect to defense spending over the next two years.

Robust economic growth: On the economy, the budget plan assumes real GDP growth of 3.2 percent this year, 3.1 percent in 2020, and then a sustained growth rate of between 2.8 and 3.0 percent for the remainder of the decade. Over the 10-year budget window, real GDP growth would average 2.9 percent.

That is far above the nonpartisan Congressional Budget Office’s (CBO) most recent economic projections released in January which peg real GDP growth at 2.7 percent this year and 1.9 percent in 2020. Over the same 10-year span, CBO predicts real GDP growth will average 1.8 percent – more than a full percentage point below the Trump administration. CBO’s numbers are generally in line with the private sector Blue Chip Economic Indicators.

That extra assumed economic growth has feedback effects on budget levels, including anticipated revenue. In fact, despite the plan’s assumption (within its baseline revenue figures) that those tax provisions in the 2017 tax cut law affecting individuals, estates, and passthrough entities that are scheduled to lapse after 2025 are instead made permanent – at a cost of $1.1 trillion within the budget window – the blueprint still predicts that revenues will bounce back to 18.1 percent of GDP by the end of the decade, a level that would exceed the 50-year average revenue level of 17.4 percent of GDP.

While it is not uncommon for an administration of either political party to assume its policies will be good for economic growth, some policymakers took issue with the extent to which this particular budget plan did so.

“It’s one thing to wish for that economic growth. It’s another thing to build your budget around it,” said Rep. Scott Peters, D-Calif., during a March 12 House Budget Committee hearing with Russell Vought, the acting director of the Office of Management and Budget.

Proposed appropriations levels could spell trouble ahead: The phrase “the president proposes and Congress disposes” is a common refrain with every presidential budget, reflecting the fact that an administration’s budget proposal is just that – a proposal. Congress can, and often does, ignore the bulk of its contents – particularly during times of divided government.

One aspect of the president’s plan that could have near-term practical import, however, is its proposals on appropriations levels for fiscal year 2020. Lawmakers, of course, struggled mightily with appropriations for current fiscal year 2019 – so much so that the government went into partial shutdown for a record 35 days during December and January. Now, absent a deal to lift the statutory sequester caps, defense appropriations will be reduced by 11 percent and nondefense appropriations by 9 percent in upcoming fiscal year 2020 relative to their enacted levels this year.

But the administration’s budget clearly signals that President Trump is neither backing down in his demand for funding for his proposed wall along the southern border – the ostensible cause of the recent government shutdown – nor showing a willingness to continue the recent bipartisan practice of lifting the sequester caps, as Democrats and Republicans have done on three separate occasions since 2013, most recently through the Bipartisan Budget Act of 2018 which boosted the caps by a total of roughly $300 billion over fiscal years 2018 and 2019.

In fact, the budget proposed this week by President Trump moves 180 degrees away from those past bipartisan deals by suggesting that nondefense appropriations (for example, on departments such as Education, State, Interior, and Treasury) be reduced to sequester levels in fiscal year 2020 and then cut by 2 percent per year after that. Those reductions would apply on a nominal basis, resulting in a roughly 40 percent cut in 2029 relative to inflation-adjusted 2019 levels – a cut of $1.1 trillion over the course of the next decade. (Within these amounts, the White House is proposing a budget bump for the Internal Revenue Service. More on that below.)
On the defense side, the administration proposes a near mirror-image increase of roughly $1 trillion over the next decade – and suggests side-stepping the need to raise the statutory caps in fiscal years 2020 and 2021 (the last two years the sequester, as it applies to discretionary spending, is scheduled to be in effect) by including the spending increases in what is known as the Overseas Contingency Operations (OCO) account that is generally designated for war-related outlays and is exempt from the statutory limits.

The administration’s budget also rekindles Trump’s demand for border wall money, asking Congress for more than $8 billion for his signature project.

The hard line taken by the president on discretionary spending sets up a likely clash with appropriators – even those from within his own party – as they contemplate negotiating a caps deal and follow-on appropriations legislation for the upcoming fiscal year.

“This one is frankly less realistic than most presidential budgets,” said Rep. Tom Cole of Oklahoma, the top Republican on the appropriations subpanel for the departments of Education, Labor, and Health and Human Services.

Of the OCO workaround for defense spending Cole noted, “[t]hat’s fine, but Congress isn’t going to accept that.”

House Budget Committee Chairman John Yarmuth, D-Ky., echoed those sentiments and predicted that Democrats and Republicans – at least those in Congress – recognize they need to come together on a fourth, and hopefully final, sequester replacement package.

“There is bipartisan consensus on Capitol Hill that we must raise the caps for both nondefense and defense discretionary spending levels. The administration’s play to delay is a total disregard for responsible governing,” Yarmuth noted in a statement released in advance of the budget.

**Tax proposals at a glance**

As already noted, the budget’s baseline revenue figures – that is, that plan’s revenue levels before adjustment for explicit budget policy – assume that the temporary provisions affecting individuals, estates, and passthrough businesses that were enacted in the 2017 tax bill and are scheduled to expire after 2025 are instead made permanent.

Based on the explanatory materials the administration released this week, the FY 2020 budget otherwise includes a handful of discrete tax proposals but does not call for sweeping changes to federal tax laws. Here is an overview of the tax provisions drawn from the limited descriptions that are available so far. (Additional details may emerge when the White House releases its analytical perspectives report and other budget materials the week of March 18.)

**Education:** A new proposal in this year’s blueprint would provide tax credits of up to $50 billion over 10 years for individuals or businesses making donations to scholarship programs for families of elementary and secondary students who are seeking state-defined public or private education options.

**Health care:** The president’s budget includes what are for the most part familiar GOP proposals to expand access to tax-preferred health savings accounts (HSAs) and medical savings accounts (MSAs) as well as tweak selected provisions in the Patient Protection and Affordable Care Act (PPACA). Specifically, the blueprint would:

- Allow Medicare beneficiaries with high-deductible health insurance plans to make tax-deductible contributions to HSAs or MSAs;
- Expand the range of high-deductible health insurance plans that can be linked to an HSA;
- Require a minimum contribution for PPACA premium tax credits; and
- Reduce the grace period for PPACA exchange premiums.

Another provision would allow individuals who receive funds for qualified tuition and related expenses under the Indian Health Service Professions Scholarship Program to exclude those amounts from income in return for an obligatory service requirement and allow a similar exclusion for loan amounts forgiven under the Indian Health Service Loan Repayment Program.

**Energy:** Like it did last year, the administration proposes to reauthorize the Oil Spill Liability Trust Fund excise tax, which most recently lapsed at the end of 2018.
But the budget proposal also includes new provisions that call for repealing several alternative energy tax incentives including:

- The qualified plug-in electric drive motor vehicle credit;
- Accelerated depreciation for renewable energy property;
- The energy investment credit;
- The credit for residential energy-efficient property; and the
- Income exclusion for utility conservation subsidies.

**IRS budget, taxpayer compliance:** The administration calls for $11.5 billion in base funding for the Internal Revenue Service, including $290 million for the Service’s ongoing efforts to overhaul its information technology infrastructure. (The fiscal 2019 budget deal that was signed into law last month provided $11.3 billion in base funding, including $150 million for information systems modernization.)

On the compliance side, the blueprint calls for separate legislation that would boost tax enforcement funding by $15 billion over the next decade – a so-called “program integrity cap adjustment” – and in so doing return a projected $47 billion to the agency in increased collections.

The blueprint also includes specific compliance and enforcement proposals to:

- Increase oversight of paid tax return preparers (last year’s proposal called for giving Treasury explicit regulatory authority);
- Give the IRS greater flexibility to address certain correctable errors on tax returns before issuing refunds;
- Clarify the worker classification and information reporting rules;
- Require taxpayers to provide Social Security Numbers to the claim child tax credit, the earned income tax credit, and the credit for other dependents; and
- Expand mandatory electronic filing of W-2s.

The bulk of these provisions are carried over from last year’s budget package.

**Mnuchin defends budget before congressional taxwriters**

Treasury Secretary Steven Mnuchin defended the administration’s budget plan before House and Senate taxwriters at separate hearings on March 14. Not surprisingly, the hearings also touched heavily on issues related to the 2017 tax cut legislation (known informally as the Tax Cuts and Jobs Act or TCJA) and the 2019 tax filing season. The Ways and Means panel also discussed the statutory debt limit – Treasury is currently employing so-called “extraordinary measures” to avoid default in the wake of the debt limit’s reinstatement on March 2 – and the anticipated request by House Ways and Means Committee Chairman Richard Neal, D-Mass., for President Trump’s tax returns.

At the Ways and Means Committee hearing, Chairman Neal focused part of his criticism on the budget’s proposed reductions in Medicare, Medicaid, and Social Security disability insurance – other programs that fall under his committee’s jurisdiction and which, at least with respect to Medicare and Social Security, President Trump pledged to hold harmless during the 2016 campaign.

“It is no coincidence that this administration is looking to cut trillions of dollars from these important programs barely a year after supporting unpaid-for tax cuts for the wealthy…,” Neal said.

But Senate Finance Committee Chairman Charles Grassley, R-Iowa, noted that the president’s budget package would achieve “significant” savings on the spending side and would build on “a robust economy, and an economy that has been strengthening following enactment of tax reform” and is “benefitting Americans across the board.”

**Infrastructure:** Neal told Mnuchin at the Ways and Means hearing that he hoped bipartisan work could move forward on a large-scale infrastructure package, given the budget plan’s expressed support for a $200 billion package in addition to a long-term surface transportation reauthorization bill that will be due before the current authorization expires at the end of fiscal year 2020.

Neither Mnuchin, nor the House lawmakers, discussed funding options for either potential infrastructure bill. In response to a question from Rep. Earl Blumenauer, D-Ore., however, Mnuchin acknowledged that President Trump has
in the past suggested he might be open to an increase in the federal tax on gasoline and diesel fuel as an option for infrastructure funding but added that no decisions have been made on that issue.

Rep. Dan Kildee, D-Mich., expressed concern about the administration’s proposal to push more responsibility for infrastructure financing onto state and local governments, noting that this would be especially burdensome to the economically distressed areas that would probably benefit most from an infusion of infrastructure spending.

Mnuchin replied that Treasury would work with taxwriters in both chambers to develop a bipartisan proposal that addresses that issue.

**SALT deduction cap:** At both hearings, debate over a Tax Cuts and Jobs Act provision that capped the deduction for state and local taxes (SALT) at $10,000 fell largely along partisan lines. Finance Chairman Grassley, for example, argued that the cap made the tax code more progressive and that repealing it would “overwhelmingly benefit millionaires and billionaires” – a sentiment shared by Ways and Means Committee Republican Tom Reed of New York.

But several Democratic taxwriters on both panels who represent constituents in high-cost areas with steep local income and property taxes told Mnuchin that the cap has translated into higher federal tax bills for many middle-class families. (Ways and Means Democrat Tom Suozzi of New York said the cap was “awful” for taxpayers in his district.)

In response to a question from Ways and Means member Brad Schneider, D-Ill., and a similar question from Finance Committee member Maria Cantwell, D-Wash, Mnuchin said the administration is “sympathetic” to the adverse impact of the SALT deduction cap in certain communities and that Treasury is “monitoring” the issue. He also told Schneider that President Trump is aware of these concerns and has said he could be open to adjusting the cap. (For prior coverage of the president’s comments, see *Tax News & Views*, Vol. 20, No. 6, Feb. 8, 2019.)

**URL:** http://newsletters.usdbriefs.com/2019/Tax/TNV/190208_2.html

**Opportunity Zones:** In contrast to the SALT deduction cap, the TCJA’s new Opportunity Zone provisions generally drew bipartisan praise at both hearings, although lawmakers wondered when Treasury would release the next round of regulations to address certain outstanding questions that have been vexing stakeholders.

Mnuchin said that the regulations are being reviewed and should be finalized within the next few weeks. In response to a question from Finance Committee member James Lankford, R-Okl., Mnuchin said that still more guidance could be released as Treasury receives feedback from the public.

**GILTI, BEAT issues:** House taxwriter Adrian Smith, R-Neb., expressed concern that Treasury regulations issued in proposed form to implement the TCJA’s Global Intangible Low-Taxed Income (GILTI) and Base Erosion and Anti-Abuse Tax (BEAT) regimes under tax code sections 951A and 59A, respectively, may be overly complicated and perhaps not consistent with legislative intent.

Smith said he has been told the regulations may be “capturing longstanding legitimate transactions which no reasonable person would consider tax-avoidance strategies as newly taxable events, which is not and certainly was not our goal.”

Mnuchin indicated he would consult with his team and consider those concerns.

**IRS budget and the tax gap:** Ways and Means Committee member Don Beyer, D-Va., asked Mnuchin why the budget proposed to beef up the Internal Revenue Service’s budget for information technology without a similar bump for compliance and enforcement efforts, which he said could go a long way toward addressing the “tax gap” – the difference between the amount of taxes owed to the government and the amount actually paid.

Mnuchin replied that upgrading the Service’s technology infrastructure to bring it into the twenty-first century is a key step to improving enforcement and reducing the tax gap. (In response to a question later in the day from Finance Committee Republican James Lankford, Mnuchin said the Service is working on an updated estimate of the federal tax gap.)

**Penalty relief for underwithholding:** Reps. Kenny Marchant, R-Texas, and Judy Chu, D-Calif., commented that a large number of taxpayers were unprepared for the changes to the tax code brought about by the TCJA and as a result inadvertently found themselves owing additional tax this year – the first filing year under the new law – because they
did not adjust their withholdings correctly. They asked that Treasury and the IRS consider reducing the threshold for imposing the underpayment penalty to 80 percent of withholding or estimated payments. The IRS previously announced that penalties will be waived this year if the taxpayer has withholding or estimated payments that total at least 85 percent of their prior-year tax liability, down from the usual 90 percent threshold.

Chu noted that under the Tax Reform Act of 1986 underpayment penalties were waived altogether in the first filing year.

Mnuchin indicated that he intends to review the issue and will make a decision about a further reduction in the penalty threshold in the coming days.

**Digital taxes:** Ways and Means Chairman Neal expressed appreciation for Treasury’s work before the Organization for Economic Cooperation and Development (OECD) with respect to international tax issues generally, and digital services tax proposals in particular – a sentiment echoed by ranking Republican Kevin Brady of Texas.

"I intend to pay close attention to those developments, especially in light of France’s recent unilateral imposition of a digital services tax,” Neal noted.

Ways and Means Republican Ron Estes of Kansas characterized proposals in some European Union nations to tax digital services as "misguided."

Mnuchin replied that “digital taxes aimed at US companies are unfair and we won’t put up with that.”

— Alex Brosseau and Michael DeHoff  
Tax Policy Group  
Deloitte Tax LLP

**No clear decisions as House taxwriters wrestle with temporary tax policy**

With the 2018 tax filing season well underway, both business and individual taxpayers are anxious to learn when – or whether – Congress will reinstate and extend some two dozen temporary tax deductions and credits that expired at the end of 2017 and a handful of others that lapsed at the end of last year; but a March 12 hearing held by the House Ways and Means Select Revenue Measures Subcommittee on the subject of temporary tax provisions did not provide much clarity.

Besides the traditional tax “extenders,” the hearing also touched on temporary tax relief for victims of natural disasters and the many elements of the 2017 tax overhaul (unofficially known as the Tax Cuts and Jobs Act or TCJA) that are due to sunset in the coming years – including most of the changes for individuals and passthrough entities.

**Addressing the TCJA provisions**

There was generally unanimity among the subcommittee members and the five witnesses that taxpayers deserve stability in the code and that temporary tax policies are less than ideal. However, the hearing also touched off some partisan remarks from the subcommittee members about the development of the 2017 tax legislation, the decision Republicans made to include mostly permanent tax relief for corporations but temporary relief for individuals and passthrough businesses, and the level of benefits provided to high-income taxpayers compared to low- and middle-class individuals.

"We must [consider TCJA modifications and extensions]...with the understanding that the corporate tax rate could never have been lowered from 35 to 21 percent without the use of fiscal gaming that shortchanges families and small businesses,” said subcommittee Chairman Mike Thompson, D-Calif., in his opening statement.

Rep. Lloyd Doggett, D-Texas, noted that while “it seems like the easiest thing in the world” to make all the individual tax breaks permanent, doing so would keep in place the new lower top tax rate and the passthrough benefit he characterized as "a special tax break for Donald Trump and his [real estate] buddies.” Doggett also criticized the
Republicans for creating what he said were 32 new temporary tax breaks in TCJA, contrary to the then-majority’s stated goal of cleaning up the tax code and eliminating the need for perennial extenders hearings.

For his part, subcommittee ranking Republican Adrian Smith of Nebraska argued in his opening statement that the TCJA was “transformative legislation” that “helped working families by doubling the standard deduction and increasing the child credit, including its refundable portion.” He noted that the 2017 law would have had an even greater impact on economic growth if the provisions for individuals, estates, and passthroughs were permanent, but that lawmakers were constrained by the budget reconciliation rules, which provided that the legislation could reduce taxes by a maximum of $1.5 trillion and could not lose revenue outside of the 10-year budget window. Smith added that the House last year approved a permanent extension of these provisions as part of its Tax Cuts 2.0 package, but the legislation was never taken up in the Senate.

**Addressing the expired extenders**

On extenders, the taxwriting panel and witnesses agreed that temporary provisions have a place in the tax code – for example, to counteract the effect of an economic downturn, address disasters or emergencies, and encourage the development of new technologies – but that Congress should consider designing provisions with more of a built-in shelf life and be more deliberate in their decisions on whether or not to renew expiring incentives. Witnesses also told the panel that routinely renewing expired provisions retroactively is not effective tax policy.

Thompson told reporters after the hearing that he believes Congress should move “as quickly as possible” to deal with the expired and expiring extenders provisions in the tax code in order to provide certainty for taxpayers, but he also said the various incentives merit additional scrutiny, and he did not provide a timeline for action in the House.

**The Republican push:** Ways and Means Committee ranking member Kevin Brady, R-Texas, told *Politico* on March 13 that that he is developing a draft tax extenders package that will make some incentives permanent but phase out or end others – a view advocated by some of the Democrats at this week’s subcommittee hearing. Brady pushed for such an approach when he was chairman but lost out to the Senate’s preference of a straight extension of all the expired provisions.

““The absolute worst case option is to extend them back and extend them forward without any reforms to the package,” Brady said. “The time is right to eliminate as many of those temporary provisions as we can.”

**The Upper Chamber:** Senate Finance Committee Chairman Charles Grassley, R-Iowa, and ranking Democrat Ron Wyden of Oregon released legislation February 28 that would retroactively renew through the end of this year the expired 2017 and 2018 extenders, while also providing targeted tax relief to businesses and individuals who suffered losses in certain federally declared disasters. (For prior coverage, see Tax News & Views, Vol. 20, No. 8, Mar. 1, 2019.)

**URL:** http://newsletters.usdbriefs.com/2019/Tax/TNV/190301_1.html

What about offsets?: Senate Republican leaders have said they are opposed to offsetting the cost of an extenders bill, but Thompson told reporters after this week’s hearing that he wants to adhere to the House Democrats’ pay-as-you-go (PAYGO) rule, which generally requires spending cuts or revenue increases to offset legislation estimated to spike the deficit.

““I want to pay for tax provisions,” Thompson said. “I’ve always felt that way.”

**Disaster relief**

Taxwriters in both parties generally agreed at the subcommittee hearing that Congress should consider adopting a permanent mechanism to provide some type of short-term tax relief to victims of presidentially declared natural disasters as opposed to the current practice of enacting legislation on an incident-by-incident basis. (A year-end GOP tax bill that cleared the House in late 2018, for example, would have provided for an automatic extension of tax filing deadlines for business and individual taxpayers in any federally declared disaster area in 2018 and beyond. That measure was never taken up in the Senate and expired as active legislation when the 115th Congress adjourned in early January.)
Dem, GOP lawmakers propose permanent New Markets Tax Credit

In other developments, Ways and Means Committee Democrat Terri Sewell of Alabama and House GOP taxwriter Tom Reed of New York introduced legislation on March 12 that would permanently extend the New Markets Tax Credit, which is currently set to expire at the end of this year. The measure also would increase annual credit allocations, index future allocations to inflation, and exempt investments under the credit from the alternative minimum tax.


A companion bill has been introduced in the Senate by Republican Sen. Roy Blunt of Missouri and Finance Committee Democrat Ben Cardin of Maryland.


The Senate measure is co-sponsored by Finance Committee Republicans Rob Portman of Ohio and Tim Scott of South Carolina, Democratic taxwriter Maria Cantwell of Washington, and Senate Minority Leader Charles Schumer of New York.

— Storme Sixeas and Michael DeHoff
Tax Policy Group
Deloitte Tax LLP

Democrats introduce carried interest legislation

House Ways and Means Committee member Bill Pascrell, D-N.J., and Sen. Tammy Baldwin, D-Wis., introduced companion bills March 13 that generally would end capital gain treatment for income from carried interests.

According to a release from Pascrell and Baldwin, the Carried Interest Fairness Act of 2019 would tax carried interest compensation at ordinary income tax rates and treat it as wage income subject to employment taxes. Capital gain treatment would continue to apply for individuals “who truly put money at risk, such as private-equity partners who invest their own money in their funds,” but “all income from managing a firm’s assets would be taxed at ordinary rates,” the release said.

URL: https://pascrell.house.gov/uploadedfiles/pascre_005_xml_carried_interest.pdf

Under current law, gains on qualified carried interests that have been held for at least three years generally are taxed as long-term capital gain. The three-year holding requirement was enacted in the 2017 tax cut legislation informally known as the Tax Cuts and Jobs Act (TCJA, P.L. 115-97). The pre-TCJA holding period was one year. Pascrell and Baldwin noted in their release that President Trump campaigned for office in part on a promise to end what he called the “carried interest loophole.”

Then-Ways and Means Committee Democrat Sander Levin of Michigan introduced similar legislation in the 115th Congress.

An official revenue estimate for the Pascrell-Baldwin proposal was not available at press time, but the news release notes that a December 2018 report from the Congressional Budget Office on options for reducing the deficit projects that taxing carried interest income as ordinary would increase federal receipts by $14 billion between 2019 and 2028.

URL: https://www.cbo.gov/budget-options/2018/54795

Co-sponsors of the House version of the bill include Ways and Means Committee Democrats Earl Blumenauer of Oregon, Brian Higgins of New York, Gwen Moore of Wisconsin, Don Beyer of Virginia, and Tom Suozzi of New York, as well as several non-taxwriters who are members of the Congressional Progressive Caucus.
Senate Finance Committee Democrat Sheldon Whitehouse of Rhode Island is a co-sponsor of the Senate companion bill, as are Democratic presidential hopefuls Kirsten Gillibrand of New York and Amy Klobuchar of Minnesota.

No Republicans in either chamber have as yet signed on as co-sponsors of the legislation.

It is currently unclear whether the legislation will be taken up in either taxwriting committee or if it instead will serve primarily as a messaging vehicle for Democrats ahead of the 2020 presidential and congressional elections.

— Michael DeHoff
Tax Policy Group
Deloitte Tax LLP