Brady outlines path forward for tax reform, Trump seeks Democratic support

As congressional Republican leaders and the Trump administration continued to talk up their tax reform agenda, House Ways and Means Committee Chairman Kevin Brady, R-Texas, revealed this week that the so-called “Big Six” tax reform negotiators will share an outline of their plan with taxwriters later this month and the White House stepped up its efforts to win support from “red state” Democrats.

Outline on the way

At one of several recent meetings on tax reform with House Republicans, Brady on September 13 laid out a schedule for his colleagues that includes release to rank-and-file members the week of September 25 of a document outlining the direction that tax reform will take. That will be followed by House passage of a fiscal year 2018 budget resolution by mid-October, and then a legislative mark-up by the Ways and Means Committee.

The Big Six – Brady, Senate Finance Committee Chairman Orrin Hatch, R-Utah, Senate Majority Leader Mitch McConnell, R-Ky., House Speaker Paul Ryan, R-Wis., Treasury Secretary Steven Mnuchin, and Economic Council Director Gary Cohn – have been working all summer to develop a single consensus blueprint for tax reform, hoping to avoid the intra-party disagreements that arose during the health care debate earlier this year. Members of the Big Six have said they intend to provide Congress with a proposed outline – what Brady described to reporters on September 13 as “a consensus document with the core elements of big, bold tax reform” – and then rely on the taxwriting committees to finalize the legislation. It is unclear exactly what level of detail will be left to Congress, but expectations are that the outline will include the basic components and then allow taxwriters to move some of the various “levers” of policy in order to determine precise tax rates, enactment dates, transition rules, and other specifics.

“The whole point of all of this is the House, the Senate, and the White House are starting from the same page and the same outline, and taxwriters are going to take it from there,” said Ryan at a House meeting on September 13.

While the taxwriting committees may be starting from the same point, however, Hatch made it clear on September 14 that the Senate Finance Committee will not necessarily reach the same conclusions as its House counterpart.

“Any forthcoming documents may be viewed as guidance or potential signposts for drafting legislation, but at the end of the day, my goal is to produce a bill that can get through this committee.” he said during a hearing on individual tax reform, adding, “[a]nyone with any experience with the Senate Finance Committee knows that we are not anyone’s rubber stamp.” (See separate coverage in this issue for additional details on the Finance Committee hearing.)

Hints and innuendo

Details of the Big Six’s tax plan remain scarce, but negotiators did drop some breadcrumbs this week on their thinking about a couple of issues – while also making it evident that there are still big decisions outstanding.

Corporate rate: President Trump, Treasury Secretary Mnuchin, and White House Legislative Affairs Director Marc Short, all said this week that the administration’s goal is still a 15 percent tax rate for businesses, but at separate events both Mnuchin and Short acknowledged that this might prove unattainable. (Congressional leaders have previously made similar comments, while noting that they are targeting a rate as low as possible.) Mnuchin said September 14 that the forthcoming outline from the Big Six will include a specific corporate rate proposal.

Passthrough rates: Short also said that he is committed to bringing the rate for passthrough entities (which currently are taxed on the individual side of the tax code) into line with the corporate rate, but Mnuchin specified that passthrough service companies, such as accounting and law firms, will not be included in such a provision.

“"If you earn money that’s clearly income – if you’re an accountant firm and that’s clearly income – you’ll be taxed at income rates – you won’t be taxed at passthrough rates,” Mnuchin said at a CNBC event on September 12. “If you’re a business that’s creating manufacturing jobs you’re going to get the benefit of that rate because that’s going to be passed through to help create jobs and better wages.”

Ways and Means Chairman Brady has said that negotiators have not yet made a final determination on the treatment of passthroughs.
Retroactivity: Mnuchin also said that negotiators are considering making the tax package retroactive to the beginning of 2017. This could have a significant impact on individual taxpayers – a fact not lost on members of Congress facing re-election in 2018 – but some analysts argue that retroactive policy, especially if enacted in the last quarter of the year, is not beneficial for the economy because businesses won’t suddenly make new hiring or investment decisions this year that would spur growth.

“Retroactive tax cuts are one of the absolute worst tax reforms one can pass,” said Maya MacGuineas, president of the nonpartisan Committee for a Responsible Federal Budget. “They do nothing to change incentives and can have very negative effects if deficit financed. Policymakers should focus on how to offset the cost of the tax cuts they want to enact, not providing tax cuts to incentivize people to do things they have already done.”

Expensing limits, interest expense deductions: Comments from various officials in recent weeks suggest that tax reform negotiators intend to scale back a proposal in the 2016 House Republican tax reform blueprint that called for 100 percent expensing in year one of most tangible and intangible assets (which the nonpartisan Tax Foundation has estimated would cost the government $2.2 trillion in lost revenue over 10 years on a static basis). Negotiators have begun referring to “unprecedented expensing” instead, signaling something more generous than current policy known as bonus depreciation but short of immediate full expensing.

Marc Short made that point even more explicitly in comments at a September 12 event sponsored by the Christian Science Monitor.

“On the expensing front, we do not believe expensing should be prioritized at the expense of rates. We’re more interested in prioritizing lower rates,” he said.

Ways and Means Chairman Brady also indicated in remarks at an event sponsored by Politico September 14 that limitations on the deduction for net interest expenses – a proposal that has frequently been paired with more generous expensing limits – also will be addressed in the forthcoming outline from the Big Six. He indicated that the provision will include some carve-outs to address the concerns of certain sectors that do not have access to capital markets.

“We will continue to work toward some changes, but in a way that creates certainty and helps us grow the economy in a big way,” he said.

Rates for upper-income individuals: President Trump this week muddied the waters on the issue of individual tax rates when he repeated a talking point on September 13 that the tax package will be focused on relief for the middle class and will not benefit the wealthiest taxpayers, but then added a new twist by appearing to suggest that the top rate could increase.

“The wealthy will be pretty much where they are. If we can do that, we’d like it,” the president said. “If they have to go higher, they’ll go higher, frankly.”

However, this does not necessarily comport with the House Republican’s 2016 tax reform blueprint or the president’s own proposals offered during his campaign or included in the statement of tax reform principles the administration released earlier this year, which have been unofficially estimated to result in lower tax bills for upper-income individuals. While Republicans have advocated scaling back or repealing some current tax incentives – such as the deductions for mortgage interest and state and local taxes – that some say disproportionately benefit wealthy households, they have also proposed cutting the top income tax rate and the rate on investment income, and repealing the estate tax and the alternative minimum tax, all of which would tend to benefit higher-income taxpayers.

Budget resolution: Chicken or egg?

Most Republicans believe tax reform will have to be done using the fast-track budget reconciliation process that allows for passage in the Senate by a simple majority rather than the three-fifths majority typically required to overcome procedural hurdles in that chamber; but for that to happen, the House and Senate must first agree to an FY 2018 budget resolution that includes reconciliation instructions authorizing a tax reform package.

The House Budget Committee passed its version of a budget resolution in late July; but a vote by the full House has been held up by members of the conservative House Freedom Caucus who are demanding to see details of the tax reform proposal first.
“We will guarantee that we have enough information before we vote for the budget,” Freedom Caucus Chairman Mark Meadows, R-N.C., told reporters September 13.

Conversely, Ways and Means Chairman Brady says the taxwriters need the budget resolution and its revenue targets in order to determine the details of a tax reform bill. A Republican headcount on the budget resolution right after Labor Day showed there were not enough votes for passage. (The Freedom Caucus includes roughly three dozen members – enough to sink the proposed budget resolution if they were to join the chamber’s Democrats in voting against the measure.) But Budget Committee Chairwoman Diane Black, R-Tenn., is pushing leadership to bring it to the floor regardless and essentially dare conservatives to oppose the vehicle for tax reform. (The House is scheduled to be out of session for a district work period the week of September 18, so the earliest possible timing for a floor vote on the budget resolution would be the week of September 25.)

On the other side of the Capitol, Treasury Secretary Mnuchin and Economic Council Director Cohn met with members of the Senate Budget Committee on September 12 to try and jumpstart the process there. According to Sen. John Thune, R-S.D., who sits on both the Budget and Finance committees, Senate Republicans are considering whether to do a “full-blown” budget like that passed by the House committee or a slimmed-down “shell” version – similar to the one used to pass the FY 2017 reconciliation instructions for the health care bill – that would simply serve as a vehicle for fast-track tax reform. The latter option is likely to face strong opposition in the House, especially from more conservative members eager to show their support for policy changes that would put the country on a path to having a balanced budget in 10 years.

Wooing the Democrats

While tax reform done using reconciliation would theoretically preclude the need for any Democratic support, the Trump administration has been making overtures to Senate Democrats that it sees as potential swing votes. Marc Short, the White House legislative affairs director, said this week that the failure this year to repeal and replace the Affordable Care Act demonstrated that Republican support in the Senate is “not reliable“ and prompted the administration to open dialogue with Democrats.

As part of that initiative, Trump invited Democratic Sens. Joe Donnelly of Indiana, Joe Manchin of West Virginia, and Heidi Heitkamp of North Dakota (along with Republican Sens. Hatch, John Cornyn of Texas, Ron Johnson of Wisconsin, and Pat Toomey of Pennsylvania) to discuss tax reform at a White House dinner on September 12. Donnelly, Manchin, and Heitkamp are the only three Democratic senators who did not sign on to a recent letter that laid out the party’s conditions for moving bipartisan tax reform legislation. All three are running for re-election next year in states where President Trump won in 2016 by sizeable majorities, and were the only Democrats who crossed the aisle to vote for Trump-nominated Supreme Court Justice Neil Gorsuch in April.

URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170804_1suppA.pdf

None of the three sits on the Finance Committee – and that panel’s ranking Democrat, Oregon Sen. Ron Wyden, commented this week that he has yet to hear from the president on tax reform and that “an awful lot of time has been frittered away” by not including his party in discussions.

Additional outreach planned: The administration’s outreach is not a one-shot effort. Last week, Trump also gave a speech in North Dakota to pitch tax reform and included Heitkamp on the Air Force One flight to the event and on the platform for his remarks. (For prior coverage, see Tax News & Views, Vol. 18, No. 30, Sep. 8, 2017.) Moreover, Vice President Mike Pence, who is from Indiana, has plans to visit his home state at least three times over the next month to talk tax reform and ramp up the pressure on Donnelly.

URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170908_1.html

In the coming weeks, the president also plans to hold as many as 13 outside-the-Beltway rallies to continue making the case for reform – once again focusing on states that he carried last year and are represented by a Democratic senator facing a competitive re-election race in 2018.

But the president this week also sent signals that he does not necessarily consider bipartisanship as essential to the tax reform process. In a September 13 meeting with the Problem Solvers Caucus in the House, which includes members of both parties, Trump reportedly told attendees that he wants to give bipartisanship on tax reform “a shot.” But he quickly added, “...if it works out, great. And if it doesn’t work out great, hopefully we’ll be able to do it anyway, as Republicans, ok?”
Republican leaders weigh in: For their part, congressional Republicans have made references to welcoming input on tax reform for their colleagues in the minority but have generally expressed skepticism that that they will receive much, if any, Democratic support.

"It most likely will get done through reconciliation," Thune said following the September 12 bipartisan dinner at the White House. "It would be great if it gets done with Democrat votes, but I don't know how you get eight Democrats to vote for something."

Ways and Means Chairman Brady likewise said at an event sponsored by Politico September 14 that "there's common ground" for Democrats and Republicans to build on when it comes to reforming the tax code. But he also pointed to President Trump's recent outreach efforts as a cautionary tale for Republicans.

"If Republicans aren't willing to unite and deliver on tax reform, he'll find someone else," Brady said.

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