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House Ways and Means Committee Approves, Senate Finance Committee Releases Respective Tax Reform Bills

Tax and Public Law and Policy, November 10, 2017

Introduction

On November 9, 2017, the House Ways and Means Committee voted on the final amendments to its comprehensive plan to reform the tax code (Tax Cuts and Jobs Act of 2017 (H.R. 1)) before voting it out of committee on a party-line vote of 24-16.

On the same day, Senate Finance Committee Chairman Orrin Hatch (R-UT) released the Senate GOP's version of the Tax Cuts and Jobs Act. Major differences from H.R. 1 include:

- One-year delay of 20% corporate rate to 1/1/19
- Interest deduction limited to 30% of EBIT instead of EBITDA
- Top individual rate of 38.5%, maintain 10% bracket, and 7 individual brackets
- Maintain $1 million cap under current law for mortgage interest deduction
- Double current exclusion for estate tax to $10 million, indexed
- Different approach to tax reform for pass-throughs
- Bifurcated repatriation rate of 10% for cash/equivalents and 5% for illiquid assets
- New base erosion and anti-abuse tax on certain entities

The Chairman's Mark is a conceptual draft, describing the changes in narrative format per Committee tradition. Finance Committee members will file amendments over the weekend and begin the mark-up on Monday afternoon with opening statements. The Chairman's Mark will be revised based on feedback received over the weekend and into Monday, with a "Modified Mark" to be released early next week and used as the base text for the mark-up and amendments.

On Tuesday, November 14, the mark-up will reconvene with a walk-through of the Modified Mark followed by amendments. The mark-up could extend throughout the week with final passage as late as Friday, November 17.

The House is expected to debate and vote on H.R. 1 on the House floor at the same time, with a vote likely on Thursday, November 16. Senate Republican leaders have indicated the week of November 27 is possible for floor consideration of its version of tax reform. Senate rules for a reconciliation bill require 20 hours of floor debate followed by a rapid-fire amendment series known as vote-a-rama.

The expectation is that the House and Senate will both appoint conferees quickly and the differences between the two bills will be worked out in a conference committee in December. Republican leaders have been adamant about meeting their ambitious deadline of sending a tax reform bill to the President's desk before adjourning for the holidays.

The chart below outlines key provisions of the Finance bill and reflects changes made to H.R. 1.

Corporate Changes Comparison Scores over 10 yrs in billions (B) *not latest	11/09/17 Senate[1]	11/09/17 House[2]	6/16 GOP Blueprint[3]	12/14 Camp Tax Act[4]
Rates	-Flat 20% rate (1/1/19); permanent (-$1329B) -Cut dividends-received deduction (80% to 65%) -Repeal special rate for personal service corps	-Flat 20% rate (1/1/18); permanent (-$1462B) -Cut dividends-received deduction (80% to 65%) -Rate of 25% on personal service corps	-Flat rate of 20%	-Flat rate of 25%, but phased in over 5 yrs (33%; 31%; 29%; 27%)
AMT	-Repeal corp. AMT (-$40B)	-Repeal corp. AMT(-$40B)	-Repeal corporate AMT	-Repeal corporate AMT
Corporate integration (reduce double tax on earnings)	-No mention	-No mention	-50% deduction for dividends and cap. gains for indiv.; no pref. rate	-40% deduction for dividends and capital gains for indiv.; no pref. rate
Expensing (full and immediate write-off of certain capital investments)	-Effective 9/28/17, 100% expensing for certain capital investments (not including used); expires 1/1/23 (-$61B) -Not for regulated public utilities (available for real property business)	-Effective 9/28/17, 100% expensing for certain capital assets + used; expires 1/1/23 (-$25B*) -Not for regulated public utilities or real property business; also not if used new floor plan financing	-Expensing for "investments in tangible property (such as equipment and buildings) and intangible assets (such as intellectual property)," but not land	-Permanent Sec. 179 small business up to $250k/yr incl property -Generally lengthen depreciation schedules by repealing MACRS to slow cost recovery
Interest expense deduction	-Deduction allowed up to 30% of pretax, post-depreciation earnings; no grandfather, start '18; if gross receipts $15mil or less, no limit (+$308B) -Indefinite carryforward -Carve-out public utilities, real property businesses -Thin cap, 110% and world group but revised (+$9B)	-Deduction allowed up to 30% of pretax, pre-depreciation earnings; no grandfather, start '18; if gross receipts $25mil or less, no limit (+$172B) -5-yr carryforward -Carve-out public utilities, real property businesses, new floor plan financing -Thin cap rule world group limit of 110% (+$34B)	-Eliminate deductions for net interest expense (allowed only to the extent of interest income, although can be carried forward) -Special rules provided for financial services companies (banks, insurance, leasing)	-Interest expense limitations apply in the context of anti-base erosion rules -Thin cap rule limits the deduction if debt level of U.S. members is more than 110% of its worldwide group
Research and development (R&D) credit	-Preserve, no mention of modifications	-Preserve, no mention of modifications	-Replace with a more effective and efficient R&D business credit	-Modify and make permanent the Sec. 41 research credit
R&D expensing (Sec. 174)	-No mention	-Require 5-year amortization after 2023	-No mention	-Repeal deduction, require 5 yr amortization
Domestic production activities	-Repeal Sec. 199 domestic production deduction effective 2019 (+$81B)	-Repeal Sec. 199 domestic production deduction effective 2018 (+$95B)	-Repeal Sec. 199 deduction	-Phased repeal of Sec. 199 deduction (down to 6% in yr 1, 3% in yr 2).
NOLs (net operating losses)	-NOLs used only to reduce net taxable income by 90% -Repeal 2-yr carryback -Special 2-yr carryback in case of certain losses -No carryforward limit -(+$170B)	-NOLs used only to reduce net taxable income by 90% -Repeal 2-yr carryback -Special 1-yr carryback in case of casualty, disaster -Carryforward + interest -(+$156B)	-NOLs can be carried forward indefinitely and increased for interest, and can be used only to reduce net taxable income by 90% -No NOL carrybacks	-NOLs used only to reduce net taxable income by 90% -Standard 2-yr carryback remains, but all special carryback rules repealed except casualty, disaster
Inventory accounting and last-in, first-out (LIFO) method	-Relaxed inventory accounting for taxpayers <$15mil gross receipts	-No mention	-Arguably superseded -Evaluate more effective treatment of inventory	-Repeal LIFO method -4-yr recapture for LIFO reserves
New markets tax credit	-No mention -Preserve '18, '19	-Terminate '18 and '19 allocations; 7-yr phase-out for credits allocated	-No mention	-Repeal by omission, since NMTC was set to expire
Historic credit	-Repeal 10% reduce 20%	-Repeal with a transition	-No mention	-Repeal rehab tax credit
Low-income housing credit	-Preserve	-No mention	-No mention	-Retain the 70% present value credit, repeal 30%

SEE PAGE 5 FOR CHART ON ADDITIONAL BUSINESS DEDUCTIONS AND CREDITS

International Changes Comparison Scores over 10 yrs in billions (B) *if not latest

	11/09/17 Senate	11/02/17 House	6/16 GOP Blueprint	12/14 Camp Tax Act
Move to territorial system for foreign sub (Fsub/CFC) income	-100% Fsub dividend exemption, except for hybrid dividends (-$216B)	-100% foreign sub dividend exemption (-$205B)	-100% exemption for dividends from Fsubs	-95% exemption for dividends from Fsubs
Deemed repatriation, one-time transition tax	-Bifurcated (10% cash; 5% remaining) effected by deduction -Due over 8 yrs (8% for each of 1st 5yrs, then 15%, 20%, 25%) -FTCs limited (+$190B)	-Bifurcated (increase to 14% cash; 7% remaining) effected by deduction -Due over 8 yrs (in equal installments of 12.5%) -can use NOLs; FTCs limited (+$223B*)	-Bifurcated 8.75% tax on cash and similar, 3.5% tax on illiquid earnings -Due over 8-yr period	-Bifurcated 8.75% tax on liquid earnings and 3.5% tax on illiquid earnings -Payable 8% each of first 5 yrs (15% in yr 6, 20% in yr 7, 25% in yr 8)
Global minimum tax to prevent base erosion, including changes to Subpart F rules	-U.S. parent taxed at 20% of global intangible low-taxed income (GILTI) of CFCs; GILTI = net CFC tested income minus 10% average aggregate bases in certain foreign tangible property with 80% deemed paid FTC (+$116B) -Deduction of 37.5% if income derived US (-$86B)	-U.S. parent taxed at 20% on half of the "high returns" of its Fsubs, with high returns defined as: (1) Fsub aggregate net income, minus (2) about 8% of basis in certain foreign tangible property, minus (3) some net interest expense -FTCs ltd to 80% (+$77B*)	-No actual or quasi-global minimum tax, but prevented base erosion by imposing border adjustments (denying deductions for imports, no tax on exports) -Bulk of the Subpart F rules repealed, with exception of the foreign personal holdco rules	-15% tax on "FBCII" that is foreign-derived (expansion of Subpart F) -25% tax on "FBCII" that is U.S.-derived (anti-round tripping) -FBCII equals the portion of foreign sub's income that exceeds 10% of its basis in depreciable tangible property
Other base erosion rules	-New base erosion and anti-abuse tax on corps with base erosion %age of 4% or more (base erosion payment to foreign affiliate divided by allowed deductions); then apply min tax of 10% modified income over basic tax -Applies if $500mil/yr average gross receipts (+$124B)	-Excise tax on deductible payments between U.S. corp and foreign affiliate (unless provided at cost) -Tax is 20% of such payments, unless foreign corp treats as ECI and some deemed expenses (no mark-up) allowed -Change to 80% FTCs OK -Applies if $100mil/yr of payments in grp (+$155B*)	-The border-adjusted tax (BAT) transforms the tax base to a destination-based consumption tax, half of which acts as an inbound tax, while the other half acts as an outbound exemption	-No mention
Offshore reinsurance	-No mention, but other rules likely impact this	-No mention, but other rules likely impact this	-BAT would be harmful if no reinsurance carve-out	-No premium deduction if affiliate not U.S.-taxed

Pass-Through Changes Comparison Scores over 10 yrs in billions (B) *if not latest

	11/09/17 Senate	11/02/17 House	6/16 GOP Blueprint	12/14 Camp Tax Act
Rates	-Indiv. can deduct 17.4% of domestic qualified pass-through business income (-$460B)	-25% rate for certain income of pass-throughs -Reduced 9% rate for first $75k (small bus.) (-$448B*)	-25% top rate for "active business income of . . . pass-through entities"	-No special rate for pass-through business income generally
Guardrails to prevent abuse of special rate	-If from pship or S corp, deduction is ltd to 50% of W-2 wages; not for service bus. if $150k+ (phased)	-Elect to apply 25% rate to 30% of income or proove portion tied to size of the partner's capital investm.	-Treat pass-throughs as having paid reasonable comp to certain owners -Details unspecified	-Not applicable
Expensing	-Sec. 179 up from $500k to $1mil begin in 2018, expand qual. prop. (-$24B)	-Sec. 179 up from $500k to $5mil to begin in 2018 (-$11B)	-Expensing presumably available to all businesses	-Not applicable
Interest expense deduction	-Interest limit computed without regard to 17.4% pass-through deduction	-Limit applies at pship lvl -If average gross receipts $25mil or less, no limit	-Presumably same limitation as for C corps	-Not applicable
Carried interest	-No mention	-3-yr holding period (up from 1-yr) for long-term cap gain (+$1.2B)	-No mention	-Taxes capital gain as ordinary by deemed loan of capital /imputed int. model
Cash method	-$5mil raised to $15mil	-$5mil raised to $25mil	-No mention	-For firms up to $10mil

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Individual Changes Comparison Scores over 10 yrs in billions (B) *if not latest

	11/09/17 Senate	11/09/17 House	6/16 GOP Blueprint	12/14 Camp Tax Act
Rates	-7 brackets (10%, 12%, 22.5%, 25%, 32.5%, 35% and 38.5%); top bracket on $1mil+ jt. incm. (-$1326B)	-Reduce 7 brackets to 4 (39.6%, 35%, 25% and 12%); top bracket on $1mil+ jt. incm. (-$1089B)	-Reduce 7 brackets to 3 (33%, 25% and 12%)	-Reduce 7 brackets to 3 (35%, 25% and 10%) -35% is surtax imposed on $450k+ joint income
Standard deduction	-Enhance standard deduction; preserve addl standard deduction; repeal personal exemptions -$12k individuals -$24k married filing joint -$18k single parents	-Enhance standard deduction; repeal additional standard deduction and personal exemptions -$12k individuals -$24k married filing joint	-Consolidate standard deduction, additional standard deduction and personal exemption for self and spouse into one -$24k married filing joint	-Consolidate standard deduction, additional standard deduction and personal exemption for self and spouse into one -$22k married filing joint
Child tax benefits	-Increase child tax credit to $1,650; substantially lift caps so many more parents can claim -Preserve child & dependent care tax credit	-Increase child tax credit to $1.6k; $1k refundable -For next 5 yrs, family flexibility and non-child dependents credit ($300) – Child and dependent care credit through 2022	-Consolidate personal exemption for children and child tax credit into one enhanced child and dependent tax credit -$1.5k for each child, w/ a refundable portion	-Increase child tax credit from $1k to $1.5k and expand to children under age 18 (not 17) -Index credit for inflation -Increase phase-out level to $627,500 joint
Earned income tax credit (EITC)	-Preserve EITC	-Preserve EITC; but new rules to reduce fraud	-Preserve EITC	-Reduce the max EITC, but rebate payroll tax
AMT	-Repeal individual AMT	-Repeal individual AMT	-Repeal individual AMT	-Repeal individual AMT
Investment income (capital gains, dividends) plus the 3.8% net investment income (NII) tax	-Index breakpoints for 15% and 20% rates using chained CPI	-No change to rates -Long-term capital gain and qualified dividend rate stays at 15% (20% for $479k and up) -Preserve NII	-Deduct 50% of net capital gains, dividends and interest income (so a top rate of 16.5%) -Keep 3.8% NII tax (assume separate repeal)	-Deduct 40% of net capital gains and dividends (so a top rate of 20%)
Retirement or savings incentives	-No change to 401(k)s and IRAs; 10% early withdrawal tax for 457(b)s; no catch-up contrib. if $500k+prior yr	-No change to pretax contribution limits for traditional 401(k)s -End backdoor Roth maneuver	-"Explore the creation of more general savings vehicles" possibly consolidating current tax incent. (401(k) & Roth)	-Cap pretax traditional 401(k)'s to half the max, remainder to after-tax Roth 401(k); expand Roth IRA; end pretax IRA
Higher education tax benefits	-No details other than that plan will preserve education relief for graduate students	-Enhance AOTC and 529s - Prohibits new contributions to Coverdells	-Simplify and consolidated education tax benefits (including 529 plans and AOTC)	-Repeal education loan interest deduction -Consolidate tax benefits -Make permanent AOTC
Estate tax and GST tax	-Double exclusion from $5mil to $10mil +inflat. -No mention of repeal	-Double exclusion from $5mil to $10mil; full repeal of both in 2024	-Repeal estate tax and generation-skipping tax	-No changes
Employer-sponsored health insurance	-No mention	-No mention	-Preserve exclusion from taxable income	-Include in taxable income for purposes of surtax
Mortgage interest deduction	-Maintain $1mil cap under existing law; repeal for home equity	-Preserve, but $500k cap for new mortgages and refinanced mortgages	-Preserve, but larger std deduction limits its value	-Preserve, but gradually reduce the cap for new mortgages to $500k
State and local tax deduction	-Eliminate for individuals -Preserve for business	-Only $10k property kept, no income or sales	-No mention, but presumably repealed	-Repeal deduction for SALT, property, sales tax
Charitable deduction	-Preserve, increase limit for some cash contribut.	-Preserve, with some limitations	-Preserve, but larger std deduction limits value	-Preserve, but larger std deduction limits value
Misc. provisions	-Preserve medical expense deduction, preserve adoption tax credit -Simplify "kiddie tax"	-Repeal medical expense deduction, change to keep adoption tax credit, moving expense deduction kept for military, no prop. casualty loss deductions		

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Other Business Revenue Raisers Scores over 10 yrs in billions (B) *if not latest

	11/09/17 Senate	11/09/17 House	12/14 Camp Tax Act
Orphan drug	-Limit credit to 50% of expenses over half of 3-yr average (+$30B)	-Repeal Sec. 45C orphan drug credit (+$54B)	-Repeal Sec. 45C orphan drug credit (+$9B)
Insurance	-Changes include capitalization of certain policy acquisition expenses, adjustment for change in computing reserves (+$27B)	-Preserve current-law treatment of deferred acquisition costs, reserves and pro-ration, but placeholder 8% life insurance income surtax	-Increase interest rate for computing life insurance tax reserves (+$24B) -Capitalize policy acquisition costs (+$12B)
Private activity bonds (PABs)	-Repeal exclusion from gross income for advance refunding bonds (+$17B)	-Effective repeal, no federal tax interest exclusion for future issuances of PABs (+$39B)	-Effective repeal, no interest exclusion for future issuances of PABs (+$24B)
Entertainment expenses	-No deduction allowed for entertainment, transportation; 50% food limit & other (+$40B)	-No deduction allowed for entertainment, transportation; 50% limit on food, drinks (+$34B)	-50% limit on food, drinks; no deduction for entertainment, transportation (+$15B)
Like-kind	-Keep Sec. 1031 for only real property (+$31B)	-Keep Sec. 1031 for only real property (+$31B)	-Full repeal of Sec. 1031 (+$41B)
Nonqualified deferred comp (NQDC)	-NQDC including certain grants of stock options included in income when no risk of forfeiture (+$13B)	-Change to preserve current-law treatment of nonqualified deferred compensation (+$0B)	-Taxes nonqualified deferred compensation when no substantial risk of forfeiture (+9B)
Renewable energy tax provisions	-Preserve PATH Act treatment	-Repeal inflation adjustment effective today for Sec. 45 production tax credit -Phase out Sec. 45 production tax credit (+$14B)	-Repeal Sec. 48 investment tax credit -Repeal Sec. 45 production tax credit for renewable electricity effective in 10 yrs
Paid-in capital	-No mention	-Contributions of money or property to a corporation or partnership in exchange for an ownership interest are taxable to the extent they are not value-for-value (+$7B)	-Repeal Sec. 118 -Contributions of land and other property by government to corporation in exchange for stock of lesser value taxed (+$9B)
U.S. territories	-No mention	-Extend Puerto Rico rum excise tax benefit (+$0.8B)	-No major Puerto Rico tax changes
Nonprofit tax changes	-(UBTI) unrelated business taxable income computed separately for each trade or business (+$3.2B) -Impose excise tax on investment income of private higher ed for $250k+ asset-per-student (+$2.5B)	-Super tax exempts such as state pension funds subject to UBTI (+$1B) -Impose excise tax on investment income of private higher ed for $250k+ asset-per-student (+2.6B*)	-Repeal tax exemption for professional sports leagues, such as the NFL (+0.1B) -Impose excise tax on investment income of private colleges and universities (+$2B)
Real estate investment trusts (REITs)	-Dividends from a REIT are qualified items of income for purposes of the 17.4% deduction at the individual level (no score)	-Would get special treatment under the new pass-through rate; maximum 25% rate on certain REIT dividends (score not specified)	-End REIT spinoffs and tax built-in gain for C-corp-to-REIT conversions (enacted) (+$6B)
Advertising cost recovery	-No mention	-No mention	-Require 50% advertising costs to be amortized (+$169B)
Bank excise tax	-No mention	-No mention	-Impose new excise tax on systemically important financial institutions (+$86B)
Publicly traded partnerships	-No mention	-No mention	-Only PTPs not taxed as corps are mining, natural resources; no financial PTPs (+$4B)
Financial products	-No mention	-No mention	-Mark-to-market for derivatives (+$16B)

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[1] For the Joint Committee on Taxation's description of the Tax Cuts and Jobs Act scheduled for mark-up by the Finance Committee, published November 9, see https://www.jct.gov/publications.html?func=startdown&id=5032. For the revenue score, see https://www.jct.gov/publications.html?func=startdown&id=5033.

[2] Four primary documents associated with the reform plan were released November 2. They are (1) the draft legislative text of the bill (available at https://waysandmeansforms.house.gov/uploadedfiles/bill_text.pdf); (2) a section-by-section summary of the major provisions of the bill, produced by Ways and Means (available at https://waysandmeansforms.house.gov/uploadedfiles/tax_cuts_and_jobs_act_section_by_section.pdf); (3) a shorter descriptive summary of the bill produced by Ways and Means (available at https://static1.squarespace.com/static/598e0867be42d6f782347394/t/59fb4a0b27ef2d9f3f9a0a12/1509640715893/WM_TCJA_PolicyOnePagers%5B7%5D.pdf); (4) and a preliminary revenue table (the so-called score) produced by the Joint Committee on Taxation (available at https://www.jct.gov/publications.html?func=download&id=5026&chk=5026&no_html=1). On November 3, the amendment in the nature of a substitute to H.R. 1 (AINS) was released (available at https://waysandmeans.house.gov/wp-content/uploads/2017/11/20171106-Amendment-in-the-Nature-of-a-Substitute-to-H.R.-1.pdf) along with an updated score from the Joint Committee on Taxation (https://waysandmeans.house.gov/wp-content/uploads/2017/11/20171106-JCT-Estimated-Revenue-Effects-of-Amendment-in-the-Nature-of-a-Substitute-to-H.R.-1.pdf). For Brady's first amendment to the AINS released November 6, see https://waysandmeansforms.house.gov/uploadedfiles/chairman_brady_amendment.pdf. For Brady's second amendment to the AINS released November 9, see https://waysandmeansforms.house.gov/uploadedfiles/chairman_amendment_2.pdf.

[3] For the text of the "A Better Way" tax reform blueprint released June 24, 2016, by House Republican leadership, see http://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf.

[4] For the text of the Tax Reform Act of 2014, introduced December 10, 2014, by former House Ways and Means Committee Chairman Dave Camp as H.R. 1, see https://www.congress.gov/113/bills/hr1/BILLS-113hr1ih.pdf. For the House Ways and Means Committee's section-by-section summary on the discussion draft of the bill released February 2014, see https://waysandmeans.house.gov/UploadedFiles/Ways_and_Means_Section_by_Section_Summary_FINAL_022614.pdf. For the Joint Committee on Taxation's technical explanation dated September 2014, see https://www.jct.gov/publications.html?func=startdown&id=4674.