Concurrent Session: Tax Reform Debate

Thursday, March 31st
11:15am – 12:30pm
Marriott Marquis, Washington DC

Moderator:
Cathy Barre, SVP-Policy & Politics, NAREIT

Panelists:
Kenneth Kies, Managing Director, The Federal Policy Group (former Chief of Staff, Joint Committee on Taxation)
Russell Sullivan, Partner, McGuire Woods (former Staff Director, Senate Finance Committee)

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Tax Reform Debate

March 31, 2016

Reality Check on the Federal Deficit

A Promising Start

“Congress passed a two-year bipartisan budget plan that avoids a default on U.S. debt… The 64-35 Senate vote early Oct. 30, following House passage two days earlier, sends President Barack Obama a bill that will extend U.S. borrowing authority until March 2017, after he leaves office.”

BNA
U.S. Avoids Debt Default as Congress Passes Fiscal Plan
October 30, 2015

A Promising Start

The Congressional Budget Office projects that the budget deal will cut the ten-year deficit by $79.9 billion.

A Surprising End

“In its final act of the year, the Senate sped to pass a $1.8 trillion bill that funds the government until October and extends sweeping tax breaks, many permanently.”

Huffington Post

Senate Passes $1.8 Trillion Spending, Tax Package To Fund Government

December 18, 2015

A Surprising End

The Congressional Budget Office projects that the year-end deal will increase the ten-year deficit by $679.5 billion.

Washington Ignores the Deficit Reality

Let me start with the economy, and a basic fact: The United States of America, right now, has the strongest, most durable economy in the world. We're in the middle of the longest streak of private sector job creation in history. More than 14 million new jobs, the strongest two years of job growth since the '90s, an unemployment rate cut in half. Our auto industry just had its best year ever. That's just part of a manufacturing surge that's created nearly 900,000 new jobs in the past six years. And we've done all this while cutting our deficits by almost three-quarters.

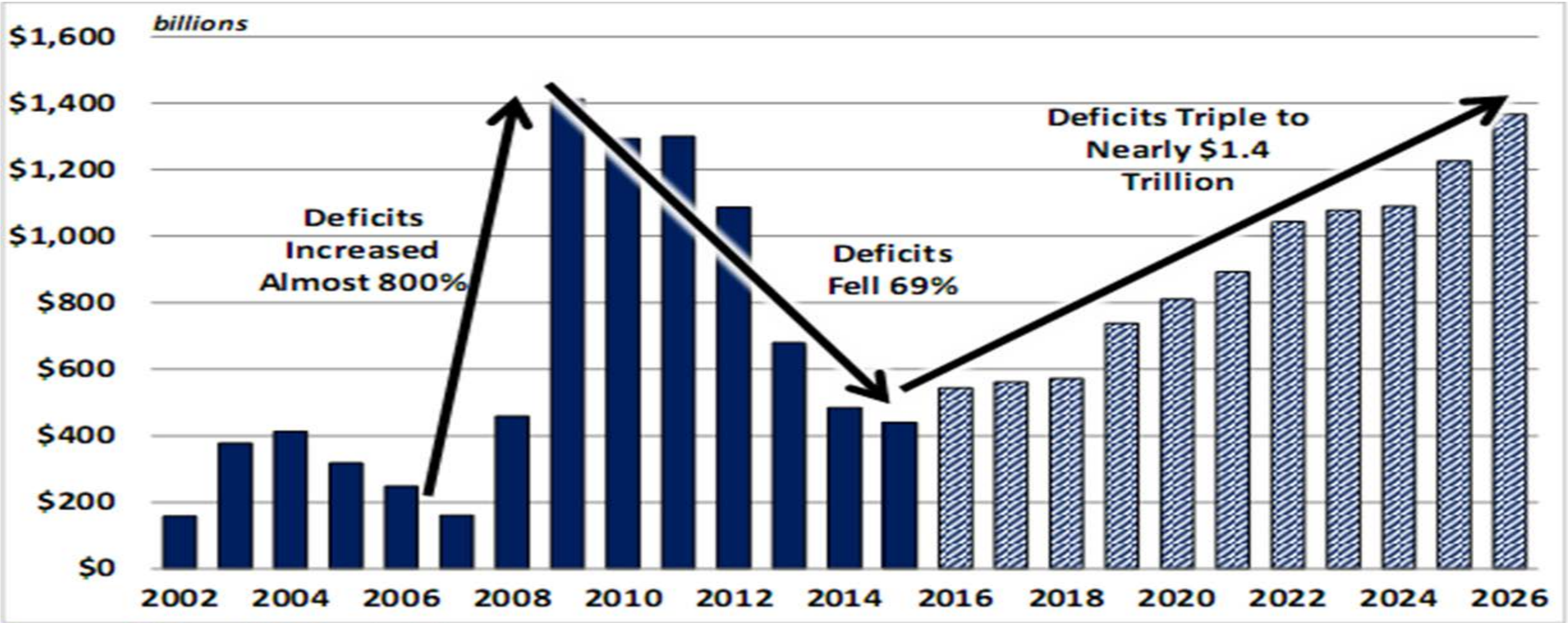
President Barack Obama
2016 State of the Union Address
January 12, 2016

Presidential Candidates are Equally Blind

“A fair summary of the debate over fiscal policy in the presidential campaign so far might go like this: Republicans spout apocalyptic but vague rhetoric about the federal debt, while proposing few if any specific spending cuts — and backing immense new tax cuts, skewed in favor of upper-income Americans. Democrats propose to expand existing entitlement programs and otherwise increase social spending, while treating deficits and the debt as yesterday’s problems, if at all.”

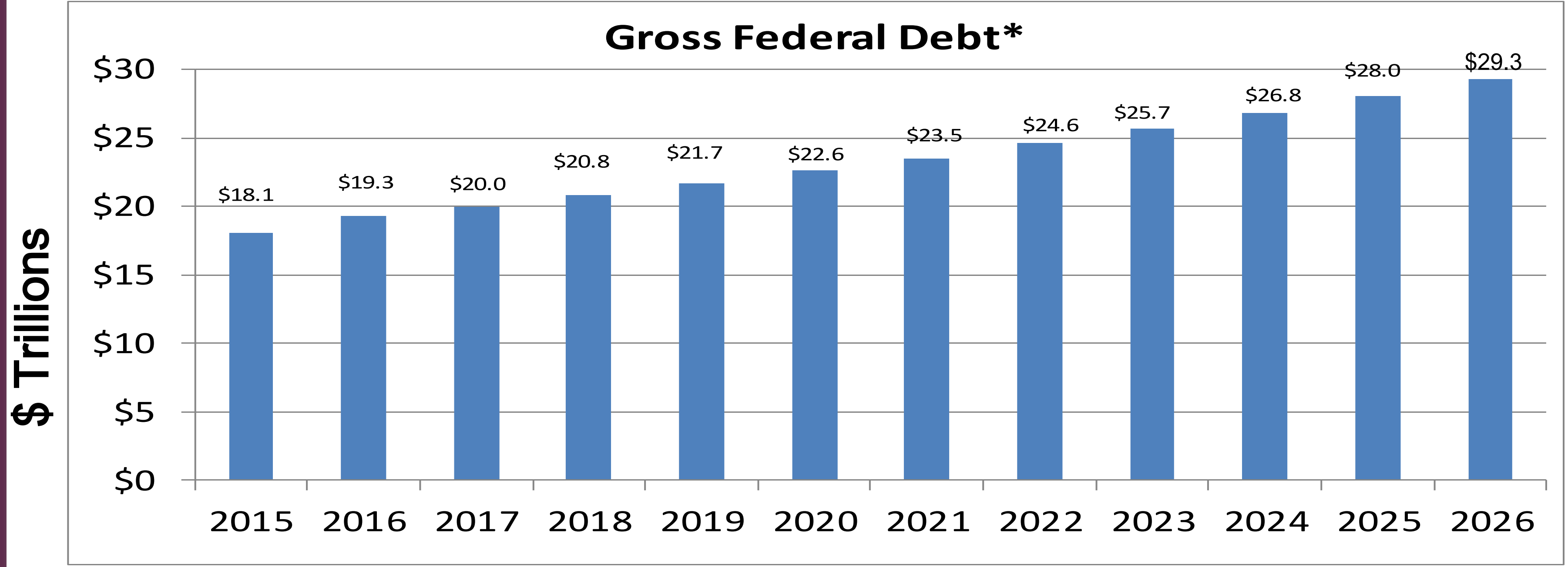
The Washington Post
The presidential candidates have one thing in common — a disregard for our debt predicament
January 20, 2016

Trillion-Dollar Deficits Set to Return by 2022



Sources: CBO and CRFB calculations

Federal Debt Outlook: CBO



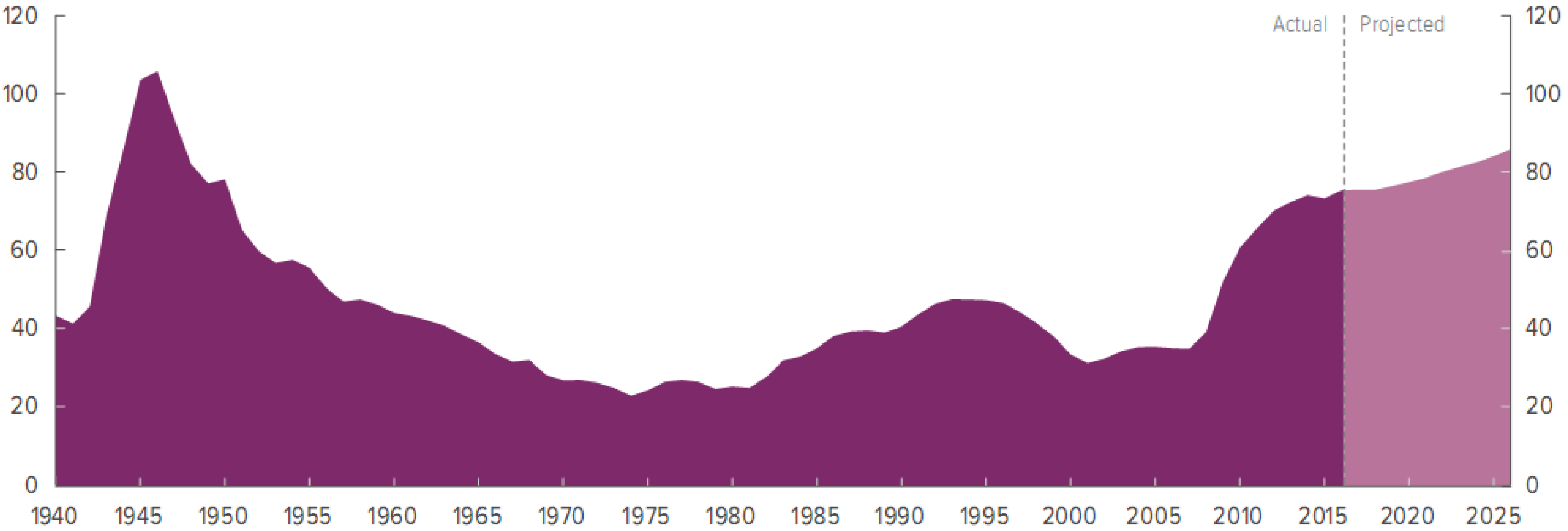
Source: CBO Baseline Budget Outlook, January, 2016

*Gross Federal Debt is Federal debt held by the public plus Treasury securities held by federal trust funds and other government accounts.

Trending Red

Federal Debt Held by the Public

Percentage of Gross Domestic Product



Source: Congressional Budget Office.

Congressional Budget Office:

83% of Total Increase in Outlays Comes from 3 Sources

Source	Percent of Total Increase From 2016 to 2026
Net Interest	**23%**
Social Security	**28%**
Major Health Programs	**32%**

Components of the Total Increase in Outlays in CBO’s Baseline Between 2016 and 2026, January, 2016

The Interest Expense Time Bomb

Percentage of Total Federal Spending that is Net Interest

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Total Spending (in trillions)	$3.6	$3.9	$4.0	$4.2	$4.4	$4.7	$4.9	$5.2	$5.4	$5.6	$6.0	$6.4
Net Interest (in billions)	$223	$255	$308	$369	$438	$498	$551	$607	$666	$719	$772	$830
Percent	6%	7%	8%	9%	10%	11%	11%	12%	12%	13%	13%	13%

Percentage Rate of Ten Year Treasury Notes

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Interest Rate	2.1%	2.8%	3.5%	3.8%	4.0%	4.1%	4.1 %	4.1%	4.1%	4.1%	4.1%	4.1%

Interest costs on federal debt are projected to grow rapidly: by 2022, they could exceed what the federal government has historically spent on R&D, infrastructure, and education combined, and could exceed them by more than three times by 2050

Source: CBO Updated Budget Projections: 2016– 2026: January, 2016

Putting the Debt in Perspective for Fiscal Year 2011

U.S. Tax Revenue:	$2,314,000,000,000
Federal Budget:	$3,597,000,000,000
New Debt:	$1,283,000,000,000
National Debt:	$14,698,625,550,307.37 (and counting)
Budget Cuts:	$38,500,000,000

Source: The Congressional Budget Office, Treasury Department's Bureau of Public Debt

Drop 8 Digits, the Debt becomes a Family Budget

Annual Family Income:	$23,140
Money Family Spent:	$35,970
New Credit Card Debt:	$12,830
Credit Card Balance:	$146,986.37 (and counting)
Budget Cuts:	$385

The Real Kicker

"A federal budget compromise that was hailed as historic for proposing to cut about $38 billion would reduce federal spending by only $352 million this fiscal year, less than one percent of the bill's advertised amount, according to the Congressional Budget Office."

- The Washington Post, April 14, 2011

Translation:

The Family Budget was cut by $3.85, not $385

Presidential Politics Commentary

Democratic Decline under President Obama

	2009	2015
Democratic Senate Seats	60	46
Democratic House Seats	257	188
Democratic Governors	28	18
Democratic State Legislative Chambers	62	30
States with Both Legislative Chambers Controlled by Democrats	27	11
Democrat State Seats Held	4082	3163
GOP State Seats Held	3223	4111

Notes:

- 2009 Senate totals as of June 2009, after Sen. Specter party switch and Sen. Frankin Seating
- Senate totals include Independents (Sens. Sanders and King) who caucus with Democrats
- House totals based on election results; total Democratic House seats varied in 111th Congress
- Nebraska's non-partisan legislature excluded from totals
- Source: National Conference of State Legislators

Democrats:

1. Clinton (67)
2. Other than Clinton, Sanders (73),

Republicans:

1. Donald Trump (69)
2. Ted Cruz (44)
3. Marco Rubio (44)
4. John Kasich (63)
5. Ben Carson (64)

Billionaires:

1. Michael Bloomberg (73)
2. Donald Trump (69)

"I'm not using donors because I'm really rich"

- Donald Trump, June 16, 2015

Tax Plans for the Presidential Candidates Still Alive

Marco Rubio Tax Reform Proposals

- Individual:
  - Three income tax brackets: 15%, 25%, and 35%
  - Eliminate itemized deductions, except charitable deduction and mortgage interest deduction
  - Cap mortgage interest deduction at $300,000 of mortgage debt
  - Enact $2,500 additional child tax credit
  - Replace standard deduction, personal exemption, and 10% tax bracket with refundable personal credit
  - Eliminate AMT
  - Reduce capital gain and QDI rate to 0%
  - Eliminate estate tax
  - Eliminate additional Medicare tax on compensation above $200,000
  - Eliminate head-of-household filing status
  - Exempt interest from income, and eliminate interest deduction (except mortgage interest), except for interest earned by financial firms

Marco Rubio Tax Reform Proposals

- Business:
  - Lower top corporate rate to 25%
  - Enact immediate investment cost expensing
  - Tax pass-through income at 25%
  - Enact credit for businesses that offer paid family leave
  - Enact territorial tax system
  - Enact one-time deemed repatriation at 6% rate
  - Excepting financial institutions, remove interest from tax base (*i.e.*, not taxable, not deductible)
  - Enact tax credit for businesses that offer paid family leave

John Kasich Tax Reform Proposals

- Individual:
  - Three income tax brackets, with a top rate of 28%
  - Retain charitable deduction and mortgage interest deduction (presumably, repeals other itemized deductions)
  - Increase EITC by 10%
  - Reduce long-term capital gain rate to 15%
  - Repeal estate tax

- Business:
  - Lower top corporate rate to 25%
  - Double value of R&D credit for businesses with less than $20 million in gross revenues
  - Enact immediate investment cost expensing
  - Enact one-time deemed repatriation at unspecified "low" rate
  - Enact territorial tax system

Donald Trump Tax Reform Proposals

- Individual:
  - Single filers earning less than $25,000 and married filers earning less than $50,000 will owe no taxes
  - Four tax brackets: 0%, 10%, 20%, and 25%
  - Eliminate AMT
  - Eliminate marriage penalty
  - Eliminate estate tax
  - Eliminate NIIT
  - Enhance personal exemption phase-out and “Pease” limitation
  - Phase-out all itemized deductions except for charitable deduction and mortgage interest deduction
  - Tax carried interest for “speculative partnerships” as ordinary income
  - Phase-out “tax exemption on life insurance interest for high-income earners” (presumably, tax “inside buildup”)

- Business:
  - Lower top “business” rate to 15% (*i.e.*, corporate and pass-through business income)
  - Enact one-time deemed repatriation at 10% rate
  - End deferral of foreign source income
  - Phase-in “reasonable” cap of interest expense deductions
  - Eliminate unspecified deductions and “loopholes”

Bernie Sanders Tax Reform Proposals

- Individual:
  - Enact 4 new tax brackets of 37%, 43%, 48%, and 52%, and raise all existing tax brackets by 2.2%
  - Cap benefit of itemized deductions at 28% for high-earning households
  - Tax capital gains and dividends as ordinary income for households making more than $250,000
  - Eliminate AMT
  - Eliminate Pease limitation and personal exemption phase-out
  - Tax carried interest as ordinary income
  - Apply Social Security payroll tax to earnings over $250,000
  - Increase top estate tax rate to 65%; lower estate exclusion to $3,500,000
  - Increase net investment income surtax to 10%
  - Tax carried interest as ordinary income

Bernie Sanders Tax Reform Proposals

- Business:
  - Lower top corporate rate to 24%
  - Enact financial transactions tax (“FTT”) at a rate between 0.005% and 0.5%
  - Enact FTT credit for low-income investors
  - End deferral of foreign-source income
  - Enact additional limits on foreign tax credits
  - Revise inversion rules to make them more stringent
  - Revise rules with respect to foreign corporations operating in the U.S.
  - Increase employer payroll tax by 6.2%
  - Enact 0.2% payroll tax to fund paid family leave

Ted Cruz Tax Reform Proposals

- Individual:
  - Establish flat tax rate of 10%
  - Lower capital gain and dividend income rate to 10%
  - Increase standard deduction by $10,000 per filer
  - Eliminate all itemized deductions other than charitable deduction and deduction for mortgage interest
  - Eliminate all credits other than EITC and CTC
  - Expand EITC by 20%
  - Eliminate estate tax
  - Enact tax-free savings accounts for up to $25,000 per year

Ted Cruz Tax Reform Proposals

- Business:
  - Replace corporate income tax with 16% business transfer tax
  - Tax pass-through income at 10%
  - Enact immediate investment cost expensing
  - Eliminate payroll tax
  - Enact territorial tax system
  - Enact one-time deemed repatriation at 10% rate

Ben Carson Tax Reform Proposals

- Individual:
  - Enact flat tax at 14.9% rate, phased-in over time
  - Enhance standard deduction and personal exemption such that income under 150% of poverty level is exempt from tax
  - Eliminate tax on social security benefits
  - Eliminate all itemized deductions
  - Eliminate all tax credits except for FTC
  - Eliminate AMT
  - Lower tax rate on capital gains and dividends to 0%
  - Eliminate exclusion for fringe benefits
  - Eliminate interest deduction or inclusion of interest in income
  - Eliminate estate tax

Ben Carson Tax Reform Proposals

- Business:
  - Lower top corporate tax rate (and rate for pass-through businesses) to 14.9%
  - Enact immediate investment cost expensing
  - Enact territorial tax system
  - Allow corporations to repatriate offshore income tax-free for six months, provided that they use 10% of the repatriated funds to create jobs for the unemployed or in enterprise zones
  - Eliminate interest deduction or inclusion of interest in income for non-financial businesses

Hillary Clinton Tax Reform Proposals

- Individual:
  - Cap benefit of itemized deductions at 28%
  - Make American Opportunity Tax Credit permanent
  - Enact $1,200 caregiver tax credit
  - Increase capital gains rate for investments held for less than 6 years to between 24% and 39.6%
  - Enact new minimum tax at 30% rate for persons earning more than $1 million
  - Enact 4% surtax on income above $5 million
  - Tax carried interest as ordinary income
  - Increase top estate tax rate to 45% and lower the deduction to $3.5 million
- Business:
  - Enact business tax credits for profit-sharing and apprenticeships
  - Enact transaction tax on high-frequency financial transactions
  - Strengthen anti-inversion rules in some specified way
  - Enact “exit tax” on foreign earnings of inverting U.S. firms

A Difficult Path to Achieving Tax Reform

Revenue Considerations:

- How Much Revenue Should Be Raised?
  - Republicans support tax reform that is revenue neutral.
  - Democrats support tax reform that raises revenue.

- How Should Tax Reform be “Scored”?
  - Republicans think that “Dynamic Scoring” is a more realistic way to score tax reform.
    - Dynamic Scoring takes into account behavioral changes and their impact on the economy.
  - Democrats think that “Static Scoring” is a more realistic way to score tax reform.
    - Static Scoring takes into account behavior changes but not their impact on the economy.

Differing Viewpoints:

- Democrats speak of "fair share" and increasing revenues
  - "The primary goals of comprehensive tax reform should be to progressively raise sufficient revenue to (1) make investments that will grow the economy, and (2) set us on a path for long-term deficit reduction. The writing is on the wall: a revenue-neutral approach to tax reform – on either the corporate or individual side of the tax code – is not an option."[1]
- Republicans speak of lowering rates and pro-growth policies
  - "The first step we can take toward overall pro-growth tax reform is to permanently lower the tax gates to allow our U.S. companies to bring their profits back home to invest in our communities, in our jobs, in our research and development, in growth."[2]

1. CONG. PROGRESSIVE CAUCUS, PROGRESSIVE PRINCIPLES FOR TAX REFORM, http://cpc-grijalva.house.gov/progressive-principles-for-tax-reform/ (last visited Mar. 1, 2016).

2. H. WAYS AND MEANS COMM., Int'l Tax Reform = More Jobs, More Growth, More Opportunity at Home (Feb. 24, 2016) (statement of Chairman Kevin Brady), http://waysandmeans.house.gov/international-tax-reform-more-jobs-more-growth-more-opportunity-at-home/.

Actions Abroad: Impact of BEPS:

- BEPS spurs U.S. leaders to action, but also companies to respond
  - “American companies competing overseas are rightly concerned that the BEPS project will result in higher foreign taxes, higher compliance costs, and double taxation. As countries around the world incorporate the BEPS ideas into their tax systems, many more companies could be forced to restructure their business operations and move U.S. activities, such as research and development, overseas.”[1]

1. H. WAYS AND MEANS COMM., Chairman Brady Opening Statement at Hearing on the Global Tax Env’t in 2016 and Implications for Int’l Tax Reform (Feb. 24, 2016), http://waysandmeans.house.gov/chairman-brady-opening-statement-at-hearing-on-the-global-tax-environment-in-2016-and-implications-for-international-tax-reform/.

Entitlement Considerations:

- Some Argue that Tax Reform is not worth doing if it doesn't reform Entitlements.
  - Between 2017 and 2026 the Federal government will spend over $32 trillion on Entitlements.
  - Entitlements is primarily funded through the payroll tax. Between 2017 and 2026 this tax is projected to raise only $13.5 trillion.
  - Entitlement spending dwarfs "discretionary" spending, which is projected to be only $12 trillion between 2017 and 2026.
  - As a percent of GDP, between 2016 and 2026, Social Security outlays are expected to increase 28% and health programs like Medicare are expected to grow 32%. Meanwhile, outlays for "discretionary" programs are expected to increase only 17% over this same time period.

Source: Congressional Budget Office's Budget Outlook, January, 2016

Pathways to Tax Reform:

- Scenario 1: Republicans retain House and Senate, and win White House
  - Result: broad-based tax reform enacted during first year of new President’s term in office.

- Scenario 2: Republicans retain House, but lose Senate and/or fail to win White House
  - Result: broad-based tax reform stalls, devolving into piecemeal “deals” to tinker with various aspects of the Code.