WASHINGTON TAX NEWS

Potomac Law Tax Newsletter—January 2017 Susan Rogers

President-elect Trump will take office on January 20, 2017. Congress convened on January 3, 2017. Based on comments from the Republican leadership and President-elect Trump, it is expected that the **Congressional agenda in the early months of 2017** will include repeal of the Affordable Care Act (ACA), tax reform, and changes to environmental regulations, as well as the confirmation hearings for several nominees for key positions in the Trump Administration and consideration of several foreign policy issues.

Senate Majority Leader McConnell (R-KY) has announced that he plans to **address tax reform and repeal of the ACA by using two budget resolutions and the budget reconciliation process**. He has stated that the first budget resolution will repeal the ACA, and a second in the spring will deal with tax reform. House Speaker Paul Ryan (R-WI) has also stated that he believes the budget reconciliation process is the best way to proceed with advancing tax reform.

The budget reconciliation procedure involves the approval of a budget resolution that sets broad tax and spending goals and instructs committees to report legislative language to meet those goals. Budget resolutions are non-binding, but budget reconciliation legislation requires the President's signature. Budget reconciliation legislation is subject to rules that limit Senate debate and bar filibusters and unrelated amendments with a simple majority needed for passage.

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Despite the stated intention of Republicans to repeal the Affordable Care Act immediately, it remains unclear whether Congressional leadership have a consensus replacement plan to include in repeal legislation — or will move instead to repeal the current law with a time certain in the future by which to pass legislation with a new plan.

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Budget Reconciliation and Tax Reform

If tax reform is passed as part of the budget reconciliation process, it must be deficit-neutral, and it will expire at the end of a 10-year period. If a narrow tax and infrastructure package is advanced, it is possible that Democratic support could be developed, but a more comprehensive tax reform package may face challenges getting the more than 60 votes needed in the Senate to prevent a filibuster. Another potential obstacle will be the position of key conservatives in Congress on the two budget resolutions, since comments have indicated that they may be willing to allow the first resolution to advance but insist on the second resolution containing proposals of importance to conservatives.

Ways & Means Committee Chairman Brady has stated that Democrats will be offered an opportunity to contribute their ideas and engage on tax reform, but he has acknowledged that Republicans will be willing to move tax reform using the budget reconciliation process.

The Senate Finance Committee

SFC Chairman **Hatch** (R-UT) has indicated that he will turn his efforts from his **corporate integration plan** to a focus on comprehensive tax reform since Republicans will control the White House and the Congress. Hatch commented, "Given the current reality, any substantive tax reform proposal will need to be considered and evaluated in the context of what has quickly become a much broader discussion." He has said that he continues to want to consider how integration fits into the tax reform debate. Chairman Hatch has also signaled that he may be reconsidering his intention to retire in 2018. Under Senate rules, he is eligible to continue as Chairman of the SFC through 2020.

The Ways & Means Committee

W&M Committee Republicans held a two-day strategy session in December to "review the decision points on tax reform and health care" and to consider the feedback they received on the GOP tax reform blueprint. Chairman Brady has downplayed the differences between the Trump tax reform proposals and the GOP blueprint by commenting that they will be the subject of discussion between the Congress and the White House and are "more than manageable." A key variance is that Trump proposes a 15% corporate rate while the blueprint calls for a 20% rate, and Trump's plan would use revenue from a deemed repatriation proposal for infrastructure spending, while Chairman Brady prefers investing that revenue into offsetting the cost of the corporate rate cut.

Miscellaneous

W&M Committee Chairman Brady and SFC Chairman Hatch introduced identical bills in the House and Senate on December 6th that would make a variety of technical changes and clarifications to provisions included in recently enacted tax legislation. The bipartisan bills were cosponsored by W&M Ranking Democrat Neal and SFC Ranking Democrat Wyden. **The technical corrections legislation** includes clarifications to current law on bonus depreciation, the research credit, the American Opportunity Credit, the partnership audit rules, and REIT income testing rules. The introduction of the bills prior to Congress recessing for the year was done to lay groundwork for the changes to be made in the new Congress and to allow taxpayers an opportunity to comment on the language of the bills.

Treasury and the IRS

The IRS issued proposed and temporary regulations under Code section 355 that provide guidance on **distributions of stock or securities of a controlled corporation without recognition of income, gain or loss**.

Treasury and the IRS issued final regulations under **Code section 367** regarding **transfers of certain intangibles (foreign goodwill and going concern value) to foreign corporations through "nonrecognition transactions."**

The IRS issued proposed regulations providing new guidance on the **fractions rule and the application of Code section 514(c)(9)(E) to partnerships that hold debt-financed real property and have one or more tax-exempt qualified organization partners as well as other partners**.

In Notice 2016-79, the IRS set the **business mileage rates for taxpayers for 2017**, which will be 53.5 cents per mile (a half-cent decrease from 2016), and set the driving rates for medical, moving and charitable purposes.

As President, Donald Trump will have significant authority over tax law and regulations, and it is expected that the new Administration and the new Congress will consider comprehensive changes to the current tax code and regulations. Although tax policy was a topic for debate and discussion during the election campaign and a Trump tax proposal was issued in September of 2015, there remains a great deal of uncertainty as to how tax legislation will develop in the first few months of the Trump Administration and what the details of that legislation will be.

Republicans control both the House and the Senate in the new Congress, which will help advance the cause of tax reform, since Republican leadership has made tax reform a priority for several years and a GOP tax reform "blueprint" was released in 2016. It should be noted, however, that proposals from the President-elect and Congressional leadership have not aligned in all areas.

Democratic staff of the Senate Finance Committee have called the House GOP blueprint regressive and fiscally irresponsible with specific criticism of the "destination-based cash flow tax" calling it "risky, untested and especially vulnerable to unforeseen consequences."

Tax Reform Update

Secretary of the Treasury Nominee, Steve Mnuchin

Steve Mnuchin, a former Wall Street executive who served as the Trump campaign finance manager, is the nominee for Secretary of the Treasury, and he has submitted tax returns and the required questionnaire to the SFC in preparation for his confirmation hearing. W&M Committee Chairman Brady praised the nomination citing his private sector experience and stated that he is looking forward to working with him on policy development to help business create jobs and grow the US economy.

In an interview after his nomination was announced, Mnuchin commented that tax reform will be his number one priority stating that it is "something that happens absolutely within the first 90 days of this presidency." He has focused on the importance of cutting the corporate tax rate, which he believes will encourage multinationals to repatriate accumulated offshore earnings and bring jobs back to the US. He believes that the revenue needed for the corporate tax rate cut as proposed by President-elect Trump to 15% will be raised by economic growth and increased personal income.

He has stated that the Trump Administration will rely on dynamic scoring to measure the revenue impact of its tax reform proposals. Dynamic scoring takes into account certain macroeconomic feedback effects of the plan on the economy and federal revenue levels. The House adopted rules in 2015 that require the Joint Committee on Taxation staff and the Congressional Budget Office to use dynamic scoring for major fiscal legislation. The Tax Foundation has estimated the revenue loss under the Trump plan to range from $2.64 trillion to $3.93 trillion using dynamic scoring, while the Tax Policy Center estimates the loss to be in the range of $6 trillion.

Border Adjustability

One of the most hotly debated issues in tax reform is the proposal in the GOP blueprint that calls for replacing the corporate income tax with a border adjustable, destination cash-flow tax that would eliminate US tax on products, services, and intangibles exported abroad, regardless of their production location, but impose a US tax on products, services, and intangibles imported into the US, regardless of their production location. Several commentators have questioned whether such a tax would comply with WTO rules.

W&M Committee Chairman Brady supports the proposal commenting that he is happy to listen to retailers, oil refiners and other critics of the plan but "it's important though for them to understand that we cannot leave in place any tax policies that encourage our companies to move their operations overseas just to sell back in the United States – those won't stay."

There is opposition to this proposal from some factions of the Republican party, who argue that border adjustments would distort the market in the long term, although some economists have suggested that adjusting exchange rates would modify the adverse effects. A letter signed by more than 75 business groups was sent to Chairman Brady stating that the proposal would lead to "huge business challenges caused by increased taxes and increased cost of goods, which would in turn likely result in reductions in employment, reduced capital investments and higher prices for consumers."

International Issues

OECD

The Organization for Economic Cooperation and Development (OECD) issued new guidance to assist in the implementation of the BEPS initiative regarding **country-by-country (CbC) reporting**. Under the BEPS Action 13 Final Report on "Transfer Pricing Documentation and Country-by-Country Reporting," the OECD is setting the reporting standards for multinational enterprises (MNEs) with cross border operations. This guidance addresses the "parent surrogate filing," the application of CbC to investment funds and partnerships, and CbC reporting notification requirements for MNE Groups during the transitional phase.

Under BEPS Action 15, the OECD released the text of a **multilateral instrument to implement tax treaty-related measures** that was negotiated by more than 100 jurisdictions with a signing ceremony set for June 2017. The new multilateral convention is expected to introduce results from the BEPS project into more than 2000 tax treaties globally.

European Commission

A summary of the arguments included in **Ireland's appeal** filed in November 2016 to overturn the August decision by the European Commission to recoup nearly $14 billion in unpaid taxes from **Apple Inc.** as part of its **state aid investigations** were publicly released. The central issue is whether two Irish tax rulings in 1991 and 2007 gave a form of special treatment to Apple. Ireland has argued that the rulings did not depart from "normal" taxation because they followed a part of the Irish tax code that states that nonresident companies should not pay income tax on profit that isn't generated in Ireland. Apple Inc. has also filed an appeal to the decision but did not release the text of its appeal. The US Treasury issued a statement about the case noting that the EU's decision is "retroactively applying a sweeping new State aid theory that is contrary to well-established legal principles, calls into question the tax rules of individual countries, and threatens to undermine the overall business climate in Europe." The General Court of the European Union will render the decision on the appeal and whether the tax must be collected.

The European Commission announced a series of **proposals to improve the Value Added Tax (VAT) environment for e-commerce businesses** in the European Union. The proposals will be submitted to the European Parliament for review and consultation, and then to the European Council for adoption. The proposals include new rules that allow companies to sell goods online to manage all their EU VAT obligations in one place, rules on actions against VAT fraud from outside the EU, and simplification of VAT rules for startups and micro-businesses selling online with cross-border sales under 10,000 euros.

For additional information and advice on these issues, please contact:

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Susan Rogers has 30 years of experience in the tax policy field in Washington including several years as Majority Tax Counsel to the House Ways & Means Committee and extensive experience managing global tax issues for a Fortune 100 multinational. Ms. Rogers' practice focuses on providing information and strategic advice to clients on US and international tax policy issues and advice on how to manage tax policy risks.