The Administration Speaks on Tax Reform (but Still without Details)

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On April 26th, President Trump released his long awaited proposal for individual and corporate tax reform. Though robust in promise, details were lacking, with a single, bulleted sheet delivered to the public (a deeper dive coming in June). Highlights included: reducing 7 personal income tax brackets into 3, doubling the standard deduction, tax relief for families with child and dependent care expenses, a 15% business tax rate (down from 35%), and a one-time tax on “trillions of dollars held overseas”.

The Trump plan joins the House Republican leadership’s own version, the “Better Way” blueprint, as Washington attempts its first major tax overhaul in thirty years. Despite what seems like a conflict, or even an overstep by Trump, Speaker Paul Ryan insists cooperation with the White House is possible. Nevertheless, significant differences exist. A border adjustment tax being pushed by House Ways and Means Chairman Kevin Brady is absent from Trump’s plan, and the House plan pegs corporate rates at 20%, instead of 15%. According to statements from the Trump White House, their plan’s rate would apply not only to corporations, but also to business income earned through pass-through entities. Treasury Secretary Mnuchin, however, acknowledged that additional rules would be required to prevent abuse of the low pass-through rate by shielding income that would otherwise be subject to ordinary rates. The House plan is less detailed on this issue.

Although not specifically addressed in President Trump’s one-page outline, the White House press briefing indicated that the deduction for state and local income or sales taxes would be among those eliminated as an offset. This deduction is especially popular with taxpayers in states with high personal income taxes such as California and New York, but may be a tempting revenue-raising target for Republicans. The House plan relies on similar deductions to be revenue neutral, in addition to the aforementioned border adjustment tax, which funds the bulk of their plan.

Additional challenges are a resistant Democratic block and deficit hawks who could block the plan if they don't get further clarity on an approach for funding the cuts. Without offsets, the Committee for a Responsible Federal Budget, in a "rough estimate", argues the White House tax plan would cost $5.5 trillion over next 10 years, while others put this closer to $7 trillion, with the debt ballooning to over 111% of GDP.

For any plan to pass, Republicans will need to employ budget reconciliation, which only requires a simple majority, as they have nowhere near the Senate votes to break a filibuster. The difficulty with this approach, however, is rules that require a budget neutral reform for permanence. Otherwise, cuts will sunset after 10 years.

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