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# ***US tax reform – buckle your seatbelts (and maybe put on a helmet)***

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***In a world of competing priorities and global risk,  
tax reform is priority #1***



**Debt Limit**



**Government Funding**



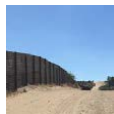
**Hurricane Relief**



**Flood Insurance Reauthorization**



**North Korea**



**Border Wall Funding**



**DACA**



**FAA Reauthorization**



**Student Loan Reauthorization**



**CHIP Reauthorization**



**NAFTA Renegotiation**

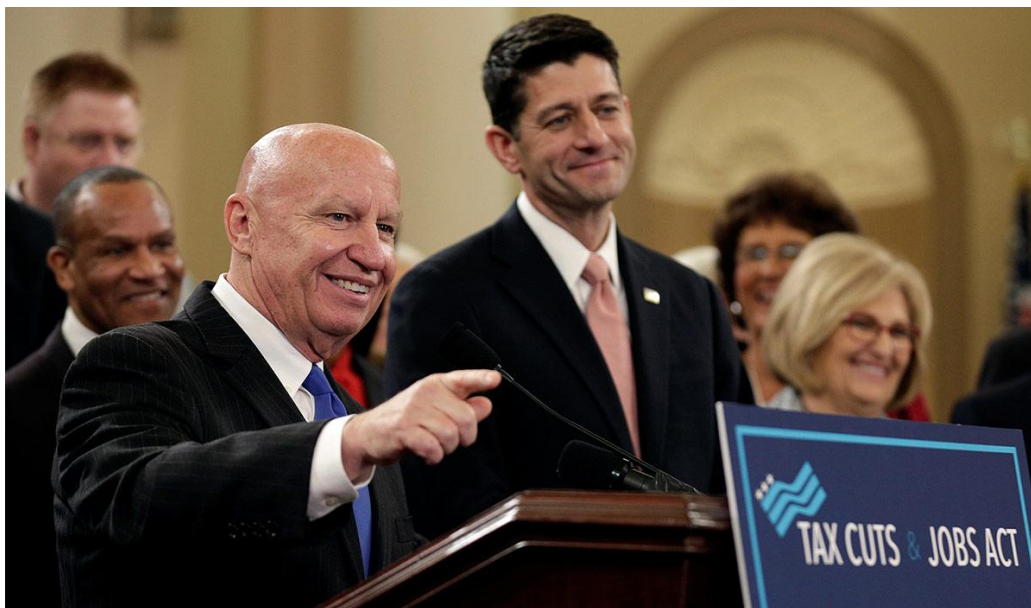


**Infrastructure Funding**

**HealthCare.gov**



# Tax Cuts and Jobs Act



## General business tax reform proposals

| Proposal                              | W&M Tax Cuts and Jobs Act (H.R. 1)   | SFC Tax Cuts and Jobs Act  | Current Law   |
|---------------------------------------|--|--|---|
| <b>Corporate tax rates/AMT</b>        | 20% rate for taxable years beginning after 12/31/2017. A blended rate applies for fiscal year taxpayers. Corporate AMT repealed after 2017   | 20% rate for taxable years beginning after 12/31/2018. A blended rate applies for fiscal year taxpayers. Corporate AMT repealed after 2017   | 35% rate and corporate AMT  |
| <b>Cost recovery (full expensing)</b> | 100% full expensing for investments made after Sept. 27, 2017 and before January 1, 2023 (additional year for certain qualified property with longer production period). Excludes property used by a regulated public utility or in a real property trade or business. Extends to used property.   | Generally the same as H.R. 1; does not expand expensing to used property.  | Recover investment over the investment's applicable life under MACRS or ADS |
| <b>Business interest expense</b>      | <p><b>Two tests would apply:</b><br/>First, limited to the sum of business interest income plus 30 percent of the adjusted taxable income (defined similar to EBITDA). Would not apply to certain regulated public utilities and real property trades or businesses.</p> <p><b>Worldwide leverage test:</b><br/>Second, limits deduction of interest by a US corporation that is part of an "international financial reporting group" (IFRG) to US corporation's share of the IFRG's EBITDA (expressed as a percentage), multiplied by 110% of the IFRG's reported net interest expense.</p> <p>Both limitations apply to both related party and unrelated party debt.</p> <p>The harsher of the two limitations will apply with disallowed interest permitted to be carried forward five years.</p> | <p><b>Two tests would apply:</b><br/>First, limited to the sum of business interest income plus 30 percent of the adjusted taxable income (defined similar to EBIT, i.e., without addback of depreciation and amortization) of the taxpayer for the taxable year. Would not apply to certain regulated public utilities and certain real property trades or businesses.</p> <p><b>Worldwide leverage test:</b><br/>Second, limits deduction of net interest expense of a US corporation that is part of a "worldwide affiliated group" to the extent the US corporation's domestic indebtedness exceeds 110% of the indebtedness it would have if its domestic debt:equity ratio were the same as that of the worldwide group.</p> <p>The harsher of the two limitations will apply with any disallowed interest carried forward indefinitely.</p> | Deductible as incurred  |

## **General business tax reform proposals (cont'd)**

| Proposal                     | W&M Tax Cuts and Jobs Act (H.R. 1)  | SFC Tax Cuts and Jobs Act   | Current Law   |
|------------------------------|---|---|---|
| <b>Pass-through entities</b> | <p>25% rate with exclusion for certain personal services businesses. Guardrails around what qualifies as business income.</p> <p>9% tax rate, phased in over 5 years, for the first \$75,000 of net business income for joint returns and \$37,500 in net business income for individuals in lieu of the 12% rate. Phased out at \$225,000 of taxable income.</p> | <p>Creates a 17.4% deduction for non-wage portion of pass-through income. (Given the 38.5% top individual rate, this is effectively a top rate of 31.8%.) Deduction is limited to 50% of individual's W-2 wages.</p> <p>The deduction does not apply to specified services business income, except when income of taxpayers married filing jointly does not exceed \$150,000 or \$75,000 for individuals.</p> | Income is passed through to the owners to be taxed at the individual rates  |
| <b>Domestic production</b>   | Repeal Section 199 deduction for taxable years beginning after 12/31/2017.  | Repeals Section 199 for taxable years beginning after 12/31/2018.   | Deduction up to 9% of qualified income for items manufactured, produced, grown, or extracted in US, exception of 6% of qualified income for oil & gas production. |
| <b>R&amp;D</b>               | <p>Maintains R&amp;D credit.</p> <p>For tax years beginning after 12/31/2022, certain Section 174 R&amp;E expenditures to be capitalized and amortized over 5 years (15 years for expenditures outside the US).</p>   | <p>Maintains R&amp;D credit</p> <p>Current law Sec. 174 retained</p>  | <p>Regular credit – 20%</p> <p>Permits the immediate deduction for research expenses under Sec. 174</p>   |
| <b>Net operating losses</b>  | Limit to 90% of income, indefinite carryforward and increase by interest factor; no carryback   | Limit to 90% of income, indefinite carryforward; no carryback   | Carryback up to 2 years and carryforward up to 20 years   |

## **International business tax reform proposals**

| Proposal                                    | W&M Tax Cuts and Jobs Act (H.R. 1)   | SFC Tax Cuts and Jobs Act   | Current Law   |
|---|--|---|---|
| <b>International tax regime</b>             | <ul style="list-style-type: none"> <li>• 'Territorial' system</li> <li>• 100% foreign dividend exemption</li> </ul>  | <ul style="list-style-type: none"> <li>• 'Territorial' system</li> <li>• 100% foreign dividend exemption</li> </ul>   | <ul style="list-style-type: none"> <li>• 'Worldwide' system</li> <li>• Foreign tax credits to mitigate double taxation</li> </ul>   |
| <b>Repatriation 'toll tax'</b>              | <p>Previously untaxed foreign earnings:</p> <ul style="list-style-type: none"> <li>• 14% cash &amp; cash-equivalents</li> <li>• 7% non-cash assets</li> <li>• Payable over 8 years</li> <li>• Proportional reduction in foreign tax credits attributable to previously untaxed foreign earnings</li> </ul>   | <p>Previously untaxed foreign earnings:</p> <ul style="list-style-type: none"> <li>• 10% cash &amp; cash-equivalents</li> <li>• 5% non-cash assets</li> <li>• Payable over 8 years</li> <li>• Proportional reduction in foreign tax credits attributable to previously untaxed foreign earnings</li> </ul>  | <p>Currently no provision. Previously untaxed foreign earnings:</p> <ul style="list-style-type: none"> <li>• 35% corporate rate when repatriated with foreign tax credit</li> </ul> |
| <b>Anti-base erosion regime (Subpart F)</b> | Subpart F generally maintained; US shareholders of CFCs subject to current 20% tax on 50% of its aggregate share of CFCs foreign high return amount (effective tax rate of 10%). An 80% foreign tax credit is permitted. In effect the minimum tax will not apply to taxpayers if, on an aggregate basis, the CFC effective foreign tax rate is 12.5% or higher. | Subpart F generally maintained; US shareholders of CFCs subject to current 12.5% US tax on "global intangible low-taxed income" (GILTI) with a deduction for foreign-derived intangible income. An 80% foreign tax credit is permitted. In effect the minimum tax will not apply to taxpayers if, on an aggregate basis, the CFC effective foreign tax rate is 15.6% or higher. Basis adjustment rules for transfers of intangible property from CFCs to U.S. shareholders. | Subpart F anti-deferral regime includes CFC's insurance income, foreign base company income, among others with foreign tax credit   |
| <b>Anti-base erosion regime (Inbounds)</b>  | 20% excise tax or similar tax on effectively connected income relating to certain outbound payments (other than interest) that are deductible, includible in cost of good sold, or includible in the basis of a depreciable or amortizable asset, made to related foreign corporations. An 80% foreign tax credit is permitted.                                  | New add-on minimum tax equal to the excess of (i) 10 percent of taxable income generally determined without regard to amounts paid or accrued to a foreign related party, including amounts includible in the basis of a depreciable or amortizable asset; over (ii) regular tax liability (determined after reduction by credits other than the R&D credit).   |   |

## Individual tax reform proposals

| Proposal  | W&M Tax Cuts and Jobs Act (H.R. 1)   | SFC Tax Cuts and Jobs Act   | Current Law  |
|---|--|---|--|
| <b>Individual rates</b>                                     | Four rate brackets (12%, 25%, 35%, 39.6%)<br><br>Phases out benefit of 12% rate for AGI exceeding \$1 million (\$1.2 million married filing joint)   | Seven rate brackets (10%, 12%, 22.5%, 25%, 32.5%, 35%, and 38.5%)   | Seven rate brackets (10%, 15%, 25%, 28%, 33%, 35%, and 39.6%)  |
| <b>Capital gain/ Qualified dividend rates (Individuals)</b> | Same as current law  | Same as current law   | Maximum 20% rate for long-term capital gains and qualified dividends                                     |
| <b>Individual – standard deduction</b>                      | \$12,200 for single filers/ \$24,400 joint returns (adjusted for inflation based on chained CPI)   | \$12,000 for single filers/ \$24,000 joint returns (adjusted for inflation based on chained CPI)                      | \$6,500 for single filers/ \$13,000 joint filers (2018)  |
| <b>Individual – itemized deductions</b>                     | No overall limitation on itemized deductions. Repeals state and local income and sales tax deductions but retains the deduction for state and local property taxes up to \$10,000                  | No overall limitation on itemized deductions. Repeals deductions for all state and local income tax and property tax. | Itemized deduction phase out begins at \$320,000 for joint filers and \$266,700 for single filers (2018) |
| <b>Estate Tax</b>   | Doubles exemption amounts until repeal of estate tax in 2024.  | Doubles exemption amounts   | Maximum 40% rate for taxable estates exceeding \$5.6 million (2018 indexed amount)                       |
| <b>Carried interest</b>                                     | Imposes a three-year holding period requirement for qualification as long-term capital gain with respect to certain partnership interests received in connection with the performance of services. | Same as current law   | Taxed at capital gains rates   |

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## Legislative paths available for tax reform in 2017

### Regular legislative process

- Benefits**
- Legislation can be enacted permanently
  - No artificial restrictions on which measures can be included
- Limitations**
- 60 votes needed at every step in the Senate (i.e., to begin debate, vote on amendments, vote on passage, to conference, etc.).

### Budget reconciliation process

- Benefits**
- Requires only simple majority vote at every step in the Senate (no filibuster allowed)
  - Expedited consideration (time limits for amendments and overall debate)
- Key Limitations**
- Legislation that increases the deficit outside of the budget window (typically 10 years) is subject to automatic sunset or other measures to avoid long term deficit effect
  - 60-vote Senate super-majority required to waive deficit rule
  - Senate rules also require reconciliation to be used only to enact measures that have a fiscal effect on the federal budget

## What is the definition of revenue-neutral?

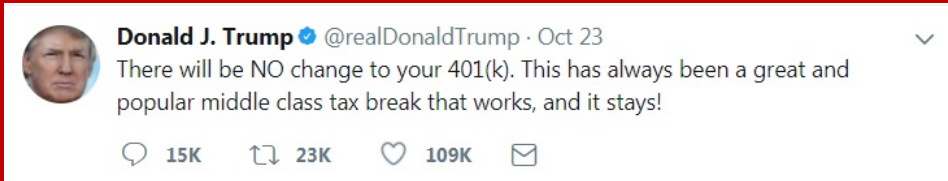
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|----------------------------|--|--|
| <b>Revenue Baseline</b>    | <b>Current-law baseline</b> assumes expiration of temporary business and individual tax provisions (“tax extenders”) and resulting increase in revenue | <b>Current-policy baseline</b> assumes renewal of tax extenders without offsets and therefore no revenue from expiration and no cost for extension.  |
| <b>Estimation Period</b>   | Congress traditionally uses <b>10-year budget window</b> to measure revenue effects of tax legislation.  | Republicans are discussing a <b>20-year budget window</b> , to extend duration of tax reductions that could be subject to automatic sunset under budget reconciliation rules.<br><br>Democrats have focused on <b>long-run sustainability</b> , meaning revenue neutrality beyond the 10-year budget window. |
| <b>Scoring Methodology</b> | <b>Conventional revenue estimation</b> , by the staff of the Joint Committee on Taxation includes behavioral responses.                                | The House has adopted <b>dynamic scoring</b> , which includes the macroeconomic growth (and revenue) effects of tax reform.  |

## 2017 Congressional calendar – key dates/deadlines

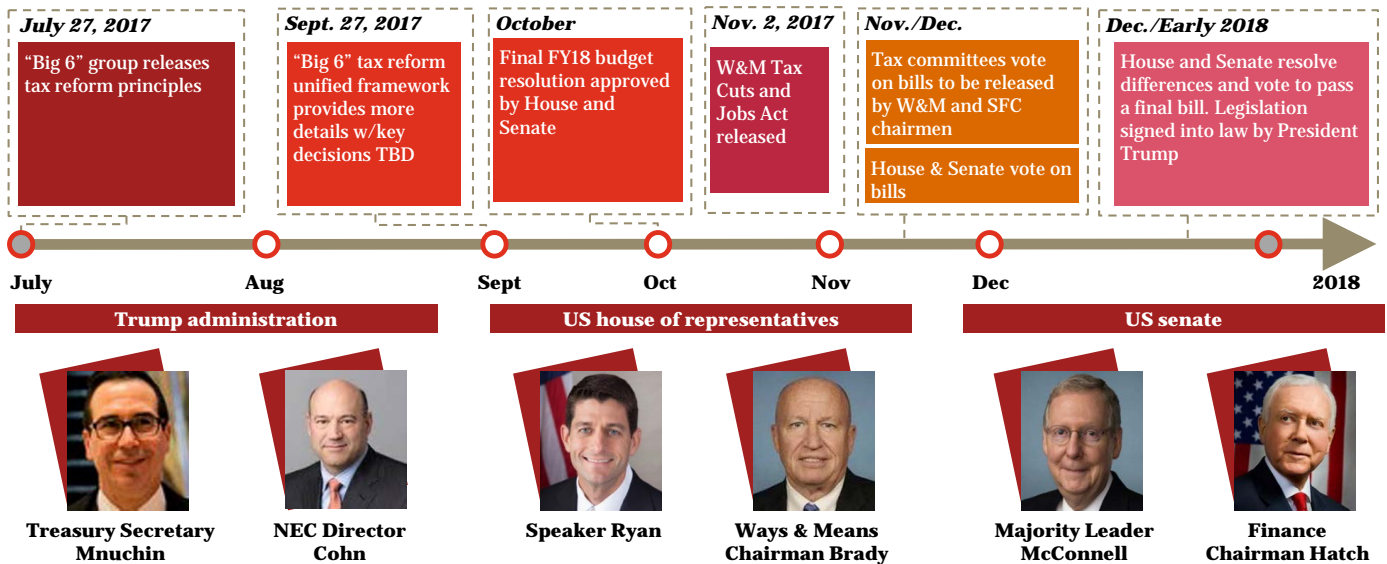
|   |                     |
|---|---------------------|
| <b>House bill released publicly</b>   | November 2          |
| <b>Revised Chairman's mark released, possibly with revenue table</b>  | November 3 – 5      |
| <b>Ways &amp; Means mark-up starts, possible Senate Finance action</b>  | Week of November 6  |
| <b>House floor consideration and vote</b>   | Week of November 13 |
| <b>Thanksgiving Recess</b>  | November 20 – 24    |
| <b>Temporary FY 2018 government funding “Continuing Resolution” (CR) and statutory debt limit suspension expires*</b> | December 8          |
| <b>Special Election Alabama Senate</b>  | December 12         |
| <b>Target adjournment</b>   | December 15         |
| <b>Medical device excise tax suspension expires; oil spill liability trust fund financing rate expires</b>            | December 31         |

\* Treasury Department retains ability to use “extraordinary measures” to meet government obligations and prevent default.

# President Trump's influence on tax reform legislative process may be a wild card



## Tax reform – A possible timeline for success



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## *Questions?*



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