

Tax Reform Update

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Tax Reform Is Really, Really Hard

- A brief journey down memory lane
- The Internal Revenue Code of 1986

Competing Visions of Tax Reform

- **Comprehensive income tax reform**
(Brady/Ryan/Camp)
- **Cut rates/eliminate deductions/broaden the base**
(Possibly Hatch and definitely various others)
- **Revenue neutral vs. deficit financed**
(Brady/Ryan vs. Hatch/Trump)

The Search for Revenue

- **Border-adjustment tax (BAT):** raises about \$1.1 trillion over 10 years if Year 1 fully phased-in.¹
- **Eliminating interest deductibility (ID):** raises about \$1.2 trillion over 10 years.²
- **Everything else** (estimates vary widely)

¹ Tax Foundation January 2017

² CNBC March 15, 2017 (citing Tax Foundation)

The Search for Revenue

- Border-adjustment tax (BAT): raises about \$1.1 trillion over 10 years if Year 1 fully phased-in.¹
 - **New BAT proposal (6/13/2017): five-year phase in. Raises about \$900 billion over 10 years.**²
- Interest deductibility (ID): raises about \$1.2 trillion over 10 years.³
- Everything else (estimates vary widely)

¹ Tax Foundation January 2017

² Tax Notes June 14, 2017 (citing Tax Foundation)

³ CNBC March 15, 2017 (citing Tax Foundation)

BAT*

- **What is it?**

*Per A.J. Auerbach (as cited by Investopedia)

BAT: What is it?

- Fully expense capital investments rather than depreciate them over a number of years or decades.
- No deduction of net interest expense against taxable income.
- Foreign profits not subject to domestic taxation.
- Make corporate income tax “destination-based” (i.e., the U.S. income tax would be border-adjustable).

Source: Tax Foundation, February 2017

What is Border Adjustment?

Imports. U.S. businesses no longer able to deduct the cost of purchases from abroad.

Exports. U.S. businesses no longer taxed on the revenue attributable to sales abroad.

Source: Tax Foundation, February 2017

BAT: Macro effects


BAT opponents


(1) $P_t \uparrow$



BAT: Macro effects

BAT proponents

(1) \$ 

(2) D_t 

Result: Trade Effect Neutral

BAT

- What is it?
- **Who loves it?**
 - **Exporters**

BAT

- What is it?
- Who loves it?
- **Who hates it?**
 - **Importers**

Eliminating ID

- **What is it?**

Eliminating ID

- What is it?
- **Who loves it?**
 - **Upper Market Companies that can pay cash and don't need to borrow.**

Eliminating ID

- What is it?
- Who loves it?
- **Who hates it?**
 - **Middle Market Companies and Small Businesses who need to borrow in order to grow.**

Organizations Opposed to Eliminating ID

- **Build Coalition.** <http://buildcoalition.org/>
 - “You can’t expense what you can’t afford.”
- **Association for Corporate Growth (ACG).**
 - “The Voice of the Middle Market.”
 - Cites RGL study that estimates \$1.1 trillion to \$2.5 trillion equity value loss for Middle Market companies.*

*<https://www.rgl.com/assets/Uploads/Documents/RGL-CIT-Analysis.pdf>

Current status

- Revenue neutrality
- BAT
- ID

Countervailing pressures

- **Repealing Obamacare (frees up \$1.2 trillion over 10 years)***

*This depends on hundreds of assumptions which may or may not be true. Forbes, March 13, 2017 (citing CBO)

Countervailing pressures

- Repealing Obamacare (frees up \$1.2 trillion over 10 years)
- **House Freedom Caucus**

Countervailing pressures

- Repealing Obamacare (frees up \$1.0 trillion over 10 years)*
- House Freedom Caucus
- **Vladimir Putin**

Timeline

- Brady/Ryan
- Hatch
- Trump
- House Freedom Caucus

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