

US - HOUSE PASSES ITS TAX BILL, SENATE UP NEXT

The House today passed its tax bill, as expected, taking an important step towards enactment of new tax legislation. The focus now shifts to the Senate that is a step behind, and where the passage of the tax bill is expected to be more challenging. Note that the Senate would not be able to pass the House bill in its current form with just a simple majority (i.e. without Democratic votes), and is continuing to work on its own bill that complies with Senate budgetary rules.

The Senate GOP released an updated version of its tax bill earlier this week that:

- 1) Repeals the Obamacare individual mandate in order to reduce federal health-care subsidies and save over \$300 billion during the 10-year budget projection period
- 2) Increases the child tax credit to \$2,000 from the initial proposal of \$1,650. The current value of the credit is \$1,000. The new proposal decreases the threshold for the credit phase out to \$500,000 for married taxpayers filing a joint return from the initial proposal of \$1 million
- 3) Lowers the proposed income tax rates further for three brackets to [22%, 24%, 32%] from [22.5%, 25%, 32.5%]
- 4) Expands the scope of the 17.4% deduction of business income for pass-throughs to include more service firms
- 5) Removes the earlier proposal of taxing employee stock options at vesting rather than when exercised

Importantly, the individual income tax cuts, increases in the child tax credit, repeal of the individual AMT, increases in the standard deduction, and the special deduction for pass-through businesses in the new Senate proposal would all expire after December 31, 2025. The reduction in the corporate tax rate to 20% would be permanent. Making the individual tax benefits temporary would allow the Senate bill to comply with the Byrd Rule that constrains the Senate bill from additional deficits after the 10-year budget projections. The Senate GOP tax bill has to comply with the Byrd rule in order to pass tax legislation with just a simple majority. According to the Joint Committee on Taxation (JCT), the new Senate proposal would lead to a budget surplus of \$30 billion in year 10, 2027, suggesting that it would satisfy the requirements of the Byrd rule.

Some of the key modifications to the Senate bill are controversial, difficult to justify politically, and further reduces the chances of any Democratic support. The changes also widen the gap between the House and Senate bills (see other key differences in ["US House and Senate tax legislation bills advance"](#), November 10, 2017). We believe that the Senate will have to make substantive changes to its bill for it to pass. The **Senate's attempt to comply with its complex budgetary rules has led to unfavorable and complicated tradeoffs.**

The Senate GOP can only afford to lose two of its members' votes assuming no Democratic support – a razor-thin margin and small room for error.

The Senate Finance Committee is expected to vote on its tax bill by tomorrow. If it passes, the plan is for the full Senate to vote on its bill the week after Thanksgiving (the week of November 27th). *(The House and Senate are going on seven and five day recesses, respectively, for the Thanksgiving holiday).* After the Senate passes its bill,

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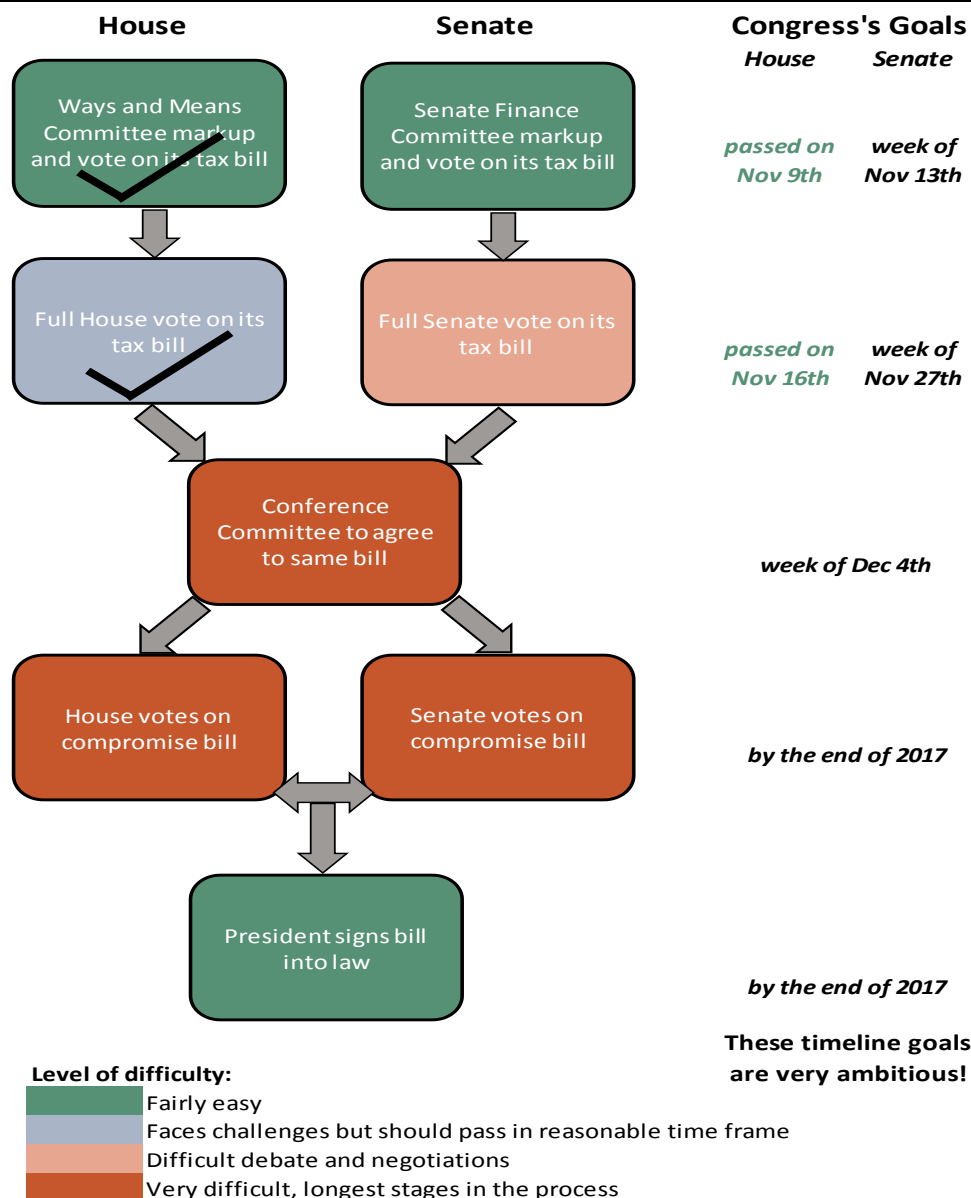
select House and Senate GOP members will have to reconcile their differences in a conference committee and agree upon a unified bill. This unified bill would then be voted upon by the House and Senate. See Figure below for an updated timeline of the tax legislation process.

There are 12 and 16 official working days left on the House and Senate calendars, respectively, this year, though leaders may add additional days/work through the holiday season if need be.

Besides the tax legislation, there are other time sensitive issues that Congress has to consider before year-end. The current Continuing Resolution expires on December 8th. If a spending agreement is not agreed upon before then, a threat of a government shutdown looms.

Tax legislation clearly has momentum, but with political obstacles, budgetary constraints, and the gap between the House and Senate bills, enactment is more likely in early 2018 than year-end.

Chart 1: Legislative Path to Tax Reform Enactment



Source: Berenberg Capital Markets

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