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Client Alert

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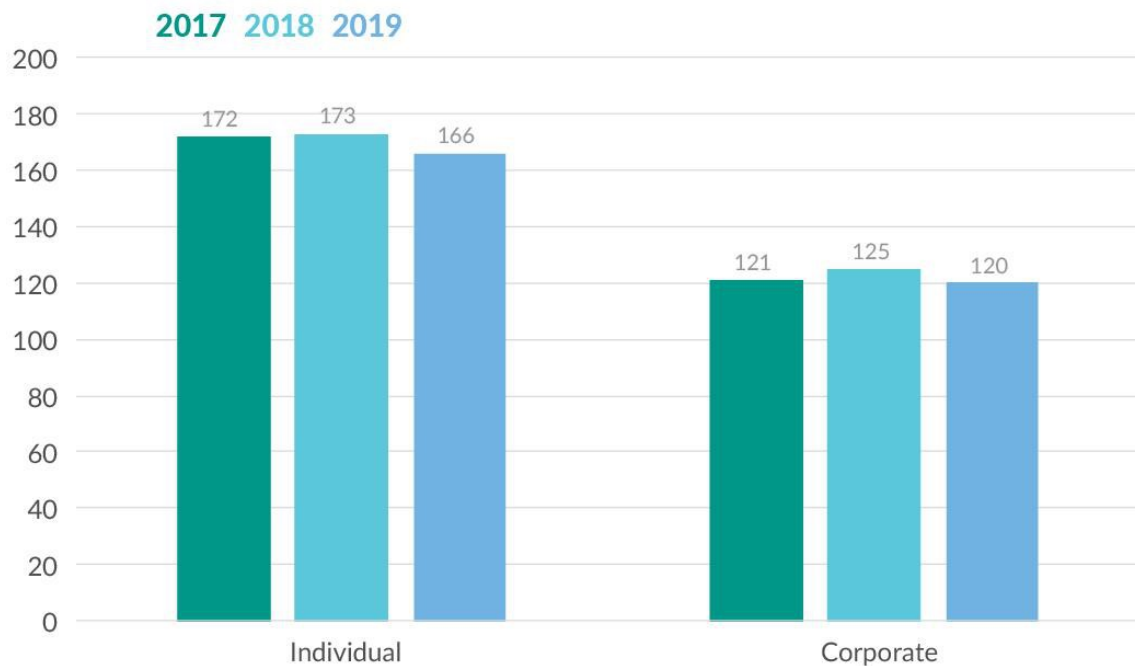
TAX TIDBIT

Welcome to the 116th Congress! Congressional members have been sworn in and are back in Washington. The big caveat — the U.S. government remains shut down for the foreseeable future as we hurtle towards tax season. Several questions remain unanswered as the new Congress kicks off — but most important — will your tax bill look different this spring? Tax Foundation conducted a study on the impact the new tax law would have on tax expenditures on the grand scale — and the answer is — largely unchanged.

Notable facts from the study include:

Tax Expenditure Numbers Remain Nearly Unchanged

Individual and Corporate Tax Expenditures Before and After the TCJA



Source: Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2017-2021",
Estimates of Federal Tax Expenditures for Fiscal Years 2018-2022.

TAX FOUNDATION

@TaxFoundation

- Cost of tax expenditures in 2018 totals \$1.5 trillion
- 86% percent of tax expenditures will go to individuals, with 14 percent going to corporations
- The largest group of expenditures will be towards health care, capital gains and dividends, and savings plans

For more information, the study can be accessed [here](#).

LEGISLATIVE LOWDOWN

Lame Duck Rewind. The lame-duck session was active for Ways and Means Republicans, who introduced a number of packages before time expired on their majority control.

The panel released a 297-page tax and oversight package (H.R.88) that included tax extenders, technical corrections, IRS reform, retirement and savings enhancements and temporary tax aid for those affected by the wildfires in California and Hurricanes Michael and Florence. The House intended to approve the package but lacked the votes to advance it for Senate consideration. Then, in early December, Ways and Means released a revised version with the "extenders" removed but again failed to advance the measure before running out of time.

The Senate confirmed Justin Muzinich 55-44 to serve as Deputy Treasury Secretary. Muzinich, nominated in April by President Donald Trump, had advised Treasury Secretary Steve Mnuchin on the TJCA. Now as his deputy, Muzinich will continue to be influential in a number of policy areas, including the implementation of last year's tax law.

Committee Priorities. Both the House Ways and Means Committee and the Senate Finance Committee will undergo membership changes in the new Congress. Here's what to expect:

- **House Ways and Means.** Chairman Richard Neal (D-MA) is expected to hold a number of hearings on the TCJA. Chairman Neal will also pursue an agenda of heavy oversight of the Trump administration's tax policies and President Trump's personal and business tax returns. If the two parties decide to work together on a comprehensive infrastructure package, Ways and Means will be expected to provide funding for the measure. Rep. Earl Blumenauer's (D-OR) push to establish a Ways & Means infrastructure subcommittee fell short in the new Congress.

As the Ways & Means ranking member, former Chairman Kevin Brady (R-TX) will be a forceful defender of the TCJA, which will be the focus of criticism by the new Ways & Means majority. Despite the expected contentious partisan atmosphere, there is room for continued bipartisan agreement on retirement issues, technical corrections and IRS reform.

- **Senate Finance.** Returning to his former post as the Senate Finance Committee chairman, Chuck Grassley (R-IA) has indicated plans to heighten scrutiny and pressure on nonprofits in the 116th Congress. In a speech on the Senate floor, Grassley noted that the broader nonprofit sector needs to be "living up to the purposes of its tax-exempt status" and be held accountable for any illicit tax shelters. Grassley has been a frequent critic of nonprofits for not providing enough public service to warrant their tax-exempt status. Grassley has also expressed an interest in pursuing additional middle-class tax cuts, working with House Democrats on changes to the Affordable Care Act and paying for a potential comprehensive infrastructure package. Republican newcomers to the committee will be Sens. Todd Young (R-IN), James Lankford (R-OK) and Steve Daines (R-MT). Daines and Lankford will also serve on the Senate Appropriations Committee, the first senators to serve on both committees since 1944.

Ranking Member Ron Wyden (D-OR) will continue his fight against the Trump administration's Treasury Department, including a slowing of the process for nominees looking to obtain Senate approval. He will also try to increase the coordination between the Treasury Department and Senate Democrats, a relationship he says could be strengthened. Sen. Bob Menendez (D-NJ), a member of the Finance panel, has already been active, blocking President Trump's nominee for IRS chief counsel Michael Desmond at the end of last session.

The Democrats will add first-term Sens. Maggie Hassan (D-NH) and Catherine Cortez Masto (D-NV) to the committee's ranks.

Brady Tries Technical Corrections One Last Time. In the waning days of the 115th Congress, outgoing Ways and Means Chairman Brady released a discussion draft — the *Tax Technical and Clerical Corrections Act* — that outlined the various technical corrections House Republicans want to fix in the TCJA. The measure was not considered and failed when lawmakers adjourned *sine die*. All is not lost, however, as Ways and Means Republicans will seek to pressure Democrats to adopt the language this session.

Looking Into Trump's Tax Returns. Now that Democrats have taken control of the House, Ways and Means Chairman Neal will be pressured by his progressive Democratic colleagues to seize President Trump's tax returns. Early indications, however, reveal that Chairman Neal is proceeding with caution. He has said he wants to wait and "lay out a case" in order to avoid accusations of looking too partisan and avoid any potential legal problems. Even for the tax writing committee, improperly disclosing tax returns to the public has serious legal consequences, so Neal is treading carefully. Speaker Nancy Pelosi, however, is singing a

different tune. Late last year, she told reporters that if the Democrats take the House, President Trump's tax returns would be "one of the first things [they would] do" and that the decision would be the "easiest thing in the world."

Neal's reluctance hasn't stopped other Democrats from introducing legislation to release presidential tax returns. Under the ethics package (H.R. 1) released last week, President Trump and Vice President Mike Pence would have to release ten years of their tax returns. Sen. Wyden, ranking member on the Senate Finance Committee, also reintroduced legislation from 2016 that would require any presidential candidate to release three years of personal tax returns. Regardless of congressional Democrats' actions, the Trump administration's Treasury Department and IRS will surely seek to delay handing anything over. Be prepared for months — or even years — of litigation intended to stall lawmakers until Republicans (the Trump administration hopes) can retake the House. And waiting in the wings would be the president's personal attorneys who would also forcefully pursue every legal remedy to stop any release of his private tax returns.

PAYING THE BILLS

Inappropriate Appropriations. As we entered the first week of 2019 and the 116th Congress, the federal government remained shut down for its third week. The stalemate is due to Congress' and President Trump's inability to come to an agreement on border security within the Department of Homeland Security (DHS) appropriation bill. The president has said he will not accept anything lower than \$5 billion to pay for a wall on the U.S. southern border — a fundamental promise of his campaign. Democrats, however, have been unwavering in their opposition to using tax dollars on a wall. House Speaker Pelosi underscored this last Thursday when she indicated that "not one dollar" of taxpayer funds will be used to build the wall.

Despite the House passing two federal appropriations bills last week to reopen the government, both parties remain at odds over funding, and it is likely that the government shutdown will at a minimum continue through the week. DHS funding was also a challenge during FY 2018 discussions. Last year, several DHS extensions were passed by Congress until the rest of the fiscal year funding was included as part of the \$1.3 trillion omnibus spending package.

While both sides continue to negotiate funding solutions, the IRS remains smack dab in the middle of the shutdown storm as the agency has now gone without funding since Dec. 21 and has since halted all routine audits. Last night, Vice President Pence and IRS officials separately stated that the agency will send out refunds during the partial shutdown and that agency's ability to process taxpayers refunds until the partial shutdown is ended. Speaker Pelosi has scheduled a House vote on Wednesday for an independent bill to extend agency resources through September and is expected to receive support from a few House Republicans. However, its odds of passing the Senate and landing on the president's desk remain slim in the short term, indicating the agency will likely remain in shutdown limbo.

This Ain't No PAYGO. The shutdown funding package passed by the House on Thursday had some opposition from the left as well as the right. Rep. Ro Khanna (D-CA) and newly elected and popular Rep. Alexandria Ocasio-Cortez (D-NY) both made statements opposing the funding package due to "PAYGO" or "pay as you go" rules. PAYGO was used in the past and is intended to prevent legislation from increasing the deficit, although Congress also gave itself an out to ignore PAYGO in certain circumstances. The various factions in the Democratic Party, notably within the House majority, may present some challenges during the party's attempts to address budgeting issues. For members objecting to the PAYGO proposal, they claim the inability to pass legislation without raising the debt limit is "terrible economics" and is "designed to hamstring

progress.” Incoming House Rules Committee Chairman Jim McGovern (D-MA), also a Congressional Progressive Caucus member, noted that PAYGO is currently required by federal law. If PAYGO rules were to be circumvented, OMB Director and Acting White House Chief of Staff Mick Mulvaney would seem to have authority to make cuts to programs. A Democratic House is unlikely to let a Republican fiscal hawk like Mulvaney have a final say on funding

GLOBAL GETDOWN

Let’s Get Digital. If 2018 was the ushering-in of a new age of online taxation, 2019 looks to become a decisive year for American tech businesses as a global effort intensifies to target overseas digital revenues.

At the end of November, the 28-country European Union failed to capitalize on its nine-month campaign to institute a 3 percent digital tax on the revenues of large tech firms profiting from business operations throughout the continent. Citing upwards of €750 million (\$858 million) in annual revenues, France, Germany, Italy, Spain and the United Kingdom were the strongest proponents of a EU-wide tax that was set to go into effect in 2021 and sunset after 10 years. The companies impacted by the tax were predominantly American, spurring backlash from numerous U.S. lawmakers and Treasury Secretary Mnuchin, who claimed the revenue tax to be a targeted attack on American tech businesses. Nevertheless, Ireland and a coalition of Scandinavian countries (i.e. Sweden, Denmark, and Finland) ultimately withdrew support for the proposal, rejecting the unanimous approval needed to enact a uniform EU digital regime.

Now, numerous countries have entered various stages of implementation and development for their own domestic digital tax. Last Tuesday, France became the first country to establish a digital tax. French Finance Minister Bruno Le Maire indicated that the tax would specifically cover direct sales, online marketplace revenues and revenues derived from the resale of private data. Several EU countries are following France’s lead as Austria, Spain and the UK formally presented similar proposals the past few weeks, while Germany continues to advocate between member-states. Moreover, the idea is picking up traction farther east, as Turkey and India have likewise introduced digital tax frameworks targeting U.S. firms for similar operational practices in their countries.

Altogether, the patchwork nature of the impending European digital tax regime in 2019 has produced an ongoing conundrum for U.S. tech companies looking to navigate between international equal treatment laws and the immediate prospects of several international levies against their business practices.

1111 CONSTITUTION AVE.

IRS Winter Reform. The 2018 Winter Solstice — or Dec. 21 for the non-meteorologists — ushered in the first official day of winter and a bad start to 2019 for the IRS. Notwithstanding the expiration of IRS funding, Dec. 21 also constituted the last day of legislative activity for the 115th Congress and with it any prospects of passing IRS reform legislation. A comprehensive tax package, spearheaded by outgoing House Ways and Means Chairman Brady, and the Taxpayers First Act of 2018 (H.R. 7227) passed the House one day before the funding deadline, but both failed to receive consideration in the Senate. However, the IRS reform provisions (H.R. 7227) passed the House with strong bipartisan support by a 378-11 vote. The legislation would have modernized IRS technology and staff policies, as well as codification of the IRS Free File program, and increased requirements for tax preparers to file online returns.

Since the bill failed to pass both chambers before the end of the last Congress, the House Ways & Means and Senate Finance committees will need to start fresh. Preexisting bipartisan support suggests the measure may provide an opportunity for bicameral support and passage in 2019. Hope springs eternal.

Wyden't You Give 'Em a Break? On Thursday, Ranking Member Wyden of the Senate Finance Committee wrote to IRS Commissioner Charles Rettig requesting the IRS to waive any penalties for filers this season for any under-withheld taxes. In the letter, Sen. Wyden stressed that the first formal filing season after the *Tax Cuts and Jobs Act* offers the opportunity for taxpayers to miss or make mistakes in their tax filings in the wake of changes to the personal exemption, itemized deductions and caps to state and local tax deductions. According to the Government Accountability Office, roughly 21 percent could be subject to underreporting their withholdings this tax season, an issue that Sen. Wyden underscored as “unavoidable” given the dilapidated state of the IRS and a tax bill that was “rushed from start to finish.” The letter concluded by requesting Rettig to comment on whether or not he believes a one-time waiver would be permitted.

AT A GLANCE

- **IRS Chief Counsel Nominee Confirmation Fails.** Sen. Bob Menendez (D-NJ) voted against Michael Desmond to be the top lawyer at the IRS, sinking the unanimous consent needed to confirm his nomination. Desmond will need to be re-nominated in the 116th Congress to fill the post.
- **W&M Infrastructure Subcommittee Fails.** In the Democratic changes to House rules for the 116th Congress, the Ways and Means infrastructure subpanel sought by Rep. Earl Blumenauer (D-OR) was not included, shooting down the effort.
- **JCT Releases Blue Book on TCJA.** The Joint Committee on Taxation released its General Explanation of Public Law 115-97, otherwise known as the Blue Book. The Blue Book is generally released once every congressional session and provides an explanation of any tax legislation enacted into law. The December 2018 publication provides an in-depth look at one piece of tax legislation — the TCJA. Expect the technical corrections included in the Blue Book to have the best chance to become enacted.
- **Chairman Neal Requests IRS Shutdown Plans.** On Friday, House Ways & Means Committee Chairman Neal wrote letters to Treasury Secretary Mnuchin and IRS Commissioner Rettig requesting information on how the IRS will maintain an orderly tax filing season amidst the ongoing government shutdown. Nearly 90 percent of all IRS staff is currently furloughed.

REGULATION STATION — ALL ABOARD

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary
BEAT	Dec. 21	REG-104259-18	42 Days	
Foreign Tax Credit	Dec. 7	REG-105600-18	28 Days	
Interest Expense Deduction	Dec. 28	REG-106089-18	49 Days	

Estate and Gift Taxes	Nov. 23	REG-106706-18	44 Days	
Sec. 956	Nov. 5	REG-114540-18	Deadline Passed Dec. 5	
Opportunity Zones	Oct. 29	REG-115420-18	Deadline Passed Dec. 28	
Sec. 965 Transition Tax	Aug. 9	REG-104226-18	Deadline Passed Oct. 9	
Debt-Equity Documentation	Sept. 24	REG-130244-17	Deadline Passed Dec. 24	
Dividend Equivalency	Nov. 5	REG-114540-18	Deadline Passed Dec. 5	
GILTI	Oct. 10	REG-104390-18	Deadline Passed Nov. 26	
SALT	Aug. 27	REG-112176-18	Deadline Passed Oct. 11	Washington Update
Passthrough Businesses	Aug. 8	REG-107892-18 Notice 2018-64	Deadline Passed Oct. 1	Washington Update
Full Expensing	Aug. 3	REG-104397-18	Deadline Passed Oct. 9	
Education Savings	July 30	Notice 2018-58	No Comment Period	Washington Update
Higher Education Excise Tax	June 8	Notice 2018-55	Deadline Passed Sept. 6	
Carried Interest	March 1	Notice 2018-18	N/A	
Health Savings Accounts	March 5	Rev. Proc. 2018-18 Rev. Proc. 2018-27	N/A	

REGULATIONS ON DECK

Due to the lapse in funding for the Treasury Department and IRS, regulations are expected to be released at a slower pace than usual, if at all, for the duration of the partial government shutdown.

BROWNSTEIN BOOKSHELF

- Ever wondered how the federal government is working to curb robocalls? Michael Pryor of Brownstein

provides a summary of recent FCC efforts to establish a reassigned numbers database.

- As Congress prepares to increase the amount of congressional oversight investigations, Greg Brower and Emily Garnett outline differences in attorney-client privilege between litigation and congressional investigations.