A Tough Road Ahead for Democrats' Ambitious Policy Agenda

By **Russell Sullivan and Radha Mohan**

President Joe Biden campaigned on a promise to address income inequality and ensure that corporations, especially those that offshore jobs, pay their fair share.

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Biden now has two years with a Democratic majority to translate his expansive campaign platform into legislation.

Before Democrats can turn to their longer-term agenda, Biden has indicated that his immediate priority will be a COVID-19 relief bill to get the nation back to work and provide support for struggling families.

Democrats are well on their way to enacting an initial relief bill — the American Rescue Plan. The U.S. House of Representatives and the U.S. Senate are poised to approve the $1.9 trillion package in the coming weeks.

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After this, Biden will pivot to his Build Back Better agenda. However, without a COVID-19-related deadline to renew certain expiring benefits, it remains to be seen whether Democrats will be able to successfully execute their ambitious agenda.

Below are three takeaways on whether the American Rescue Plan lays a solid foundation that Democrats can build on for the next package, how the next bill might unfold, and whether the proposed policies will have the intended effects.

1. Only a Band-Aid Fix

On Feb. 19, the House Budget Committee unveiled a draft of Biden's American Rescue Plan, which focuses on funding for public health measures, such as vaccine distribution, as well as reopening schools and child care facilities. The bill also includes the following tax and economic priorities:

- $1,400 in additional direct payments to individuals;
- Expansion and extension of the Families First Coronavirus Response Act's paid leave and sick leave credits;
- Extension of the employee retention tax credit;
- $15 minimum wage, which is unlikely to be included in the final package due to a lack of support;

- Increases to the child and dependent care tax credit and the child tax credit;
- COBRA subsidies and enhanced premium tax credits;
- Larger childless earned income tax credit;
- Continuation of enhanced unemployment insurance benefits; and
- Funds for small businesses and for state and local governments.

The package is intended to be a short-term solution to help individuals and businesses continue to weather the pandemic, until widespread vaccination allows the economy to fully reopen. However, it is unclear if the policies will be able to stem damage to the economy.

On the individual side, the American Rescue Plan is a carefully structured benefits package to address major pandemic-related issues such as unemployment, income insecurity, spending decreases, the need for better workforce supports, especially for women, and lowering the cost of health care.

To address joblessness, it provides generous unemployment benefits, though it does not include automatic triggers so that individuals are not reliant on Congress to continually pass relief. Without automatic triggers, individuals will once again face an unemployment benefits cliff, particularly if high unemployment rates continue through 2021 due to the ongoing effects of the virus.

In order to increase consumer spending, stimulate the economy and help families endure the effects of the pandemic, the package's biggest ticket item is $1,400 stimulus checks for individuals and dependents.

The payments phase out between $75,000 and $100,000 of adjusted gross income for individuals and $150,000 and $200,000 for joint filers. No payments can go to individuals making more than $100,000 or couples making more than $200,000.

Payments may be issued based on 2019 or 2020 income — this will allow taxpayers who have experienced declines in income or pandemic-related job loss to claim a larger payment by quickly filing their 2020 tax returns.

It is unclear if these measures will be enough to boost consumer spending until the economy fully reopens, which is not expected to happen until December.

For caregivers, the American Rescue Plan would enhance the child tax credit for a year, from $2,000 for children under 17, to $3,600 for children under 6 and $3,000 for all other children under 17.

It would also allow for advance payments of the credit starting in July, which helps low-income women who have left the workforce return to their jobs by offsetting the cost of care.

It would also change the child and dependent care tax credit for 2021 from $3,000 in qualifying expenses to $8,000 for one child, and from $6,000 to $16,000 for two or more children, as well as imposing a phaseout threshold at $125,000, completely eliminating the credit for incomes above $400,000.

The maximum credit amount would go up from 35% of qualifying expenses to 50%.

Biden's child and dependent care tax credit proposal marks a major shift in tax philosophy. Previously, the benefits of this tax credit went to families across the income spectrum, resulting in a low credit value that does not reflect the true cost of child care expenses, which are about $12,000 per year.

However, by capping the income threshold, the Biden proposal would concentrate federal dollars on those who have the most need for the credit. The targeted nature of the caregiving credits reflects the priorities in the broader Democratic agenda — fixing income inequality by providing essential workforce supports to low- and middle-income populations.

On the health care front, the American Rescue Plan also helps workers who have recently lost employer-provided health care. COBRA provides an 18-month stopgap for employees who lost their employer-sponsored coverage after a qualifying event such as a layoff or furlough.

COBRA is generally very expensive for employees since they must pay the cost of the entire insurance premium, including the employer's portion, in addition to an administration fee. The American Rescue Plan includes an 85% COBRA subsidy.

The package also includes increases to the premium tax credit. Individuals who received unemployment compensation would have access to Affordable Care Act premium tax credits, regardless of income.

Together, the two health care provisions give laid-off employees and self-employed workers health security, even if they lose their jobs or must significantly reduce hours due to the pandemic. This is particularly important to help stop the spread of COVID-19 and fully reopen the economy.

The individual provisions in the package are a start for Democrats to address income inequality and provide workforce supports that cost low- and middle-income Americans a large portion of their earnings. However, even at $1.9 trillion, the package only provides relief for a year.

At best, the American Rescue Plan will serve as a quick fix. The ultimate success of these policies and their ability to make an impact on target populations is dependent on whether Democrats can achieve permanence or at least a longer-term extension in the next package.

Furthermore, even if the provisions boost consumer spending and provide economic security, the lack of aid for hard-hit industries could result in a failure to adequately stem damage to the economy, potentially jeopardizing the rest of the Democratic agenda.

2. A Flawed Foundation

While the American Rescue Plan at least starts to address Democrats' individual tax priorities, it misses the mark on business relief, doing little to help industries that have been decimated by the pandemic.

On the tax front, the only item in the American Rescue Plan for businesses is a short-term extension of the employee retention tax credit. The bill extends the credit through the end of the year, but makes it refundable only against the 1.45% hospital tax — instead of the 6.2% old age, survivors and disability insurance tax — in order to circumvent a potential problem with the Byrd rule, which governs budget reconciliation bills.

Under current law, employers could receive an advance credit by simply using funds that would normally be withheld to cover the employees' qualified wages. At 6.2% withholding, employers are often able to cover a large portion of employee wages through withholding, allowing them to monetize the credit immediately.

However, with the change, the tax credit could be much greater than tax liability. Therefore, more employers will have to wait to receive a check from the IRS, delaying the timing and potentially the value of the benefit for cash-strapped businesses.

The American Rescue Plan's failure to include any tax incentives in anticipation of a return to work is problematic for struggling businesses. For example, proposals that once shared bipartisan support such as the cleaning credit or a rehiring credit are not included. Employers have no way to offset increased business costs, at a time when gross receipts are far below pre-COVID-19 norms.

In lieu of direct assistance, the bill focuses on general business supports. While money for vaccines, state and local governments, and education will help businesses return to normalcy and have their workforce return full time, for some hard-hit industries, even larger businesses need more aid.

For those in hospitality, travel, restaurants and gaming, a return to normalcy will not be immediate. Even as revenue stabilizes in other industries, these sectors will lag behind for at least another year. Yet, these industries will likely have to wait for future packages for any aid, at which point it might be too late to stave off further layoffs.

Furthermore, if future reconciliation bills include corporate tax increases, this could further harm recovery.

Ultimately, a failure to stabilize these industries could potentially have a negative impact on achieving Biden's long-term goals for job creation and economic revitalization.

3. Conflicting Goals and Policies in a Second Reconciliation Bill

Democrats' ability to make a lasting impact on the policy landscape hinges on a second reconciliation bill. However, if past is precedent, it will be difficult for Democrats to be able to pass two budget reconciliation bills this year, especially without the unifying factor of a COVID-19 benefits-cliff deadline.

In 2017, Republican efforts at two reconciliation bills quickly fell apart when former Sen. John McCain, R-Ariz., joined Sens. Lisa Murkowski, R-Alaska, and Susan Collins, R-Maine, to vote against repealing the Affordable Care Act. With a 51-50 majority in the Senate, Democrats cannot afford to lose even a single vote.

Furthermore, looking at a history of budget reconciliation bills since the incorporation of the Byrd rule in 1990, Congress has only been able to successfully pass two reconciliation bills once.

In 2006, Congress passed House Concurrent Resolution No. 95, which led to the enactment of the Deficit Reduction Act of 2005 (P.L. 109-171) and the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222), three months apart.[1]

Both bills received some degree of bipartisan support, with at least a few members crossing party lines.

Democrats might initially try for bipartisan legislation for certain policy priorities. However, given the partisan nature of certain policies, it is likely that Democrats will try for two reconciliation bills this year, with the next package focusing on the president's Build Back Better agenda.

This will include three major planks — infrastructure investments, green energy and domestic manufacturing incentives. It will also build upon the individual relief provided in the first bill and seek to make those provisions permanent, paid for by corporate tax rate increases, a repeal of oil and gas tax breaks and increases in taxes on the wealthy.

The driving force behind the Build Back Better agenda is job creation.

Biden's $2 trillion infrastructure plan includes investments in traditional projects such as roads and bridges, as well as electricity grids, public transportation and universal broadband.

It also includes shoring up domestic auto manufacturing, creating a carbon pollution-free power sector by 2035, and revitalizing abandoned coal, hard-rock and uranium mines to create new union jobs.

Infrastructure plans are traditionally bipartisan and this is an area where both parties might work together, though finding pay-fors will be a challenge.

Built into Biden's infrastructure plan is a push for green energy goals and incentives. In addition to what was outlined in his campaign platform, proposals like the House Democrats' Growing Renewable Energy and Efficiency Now Act will be considered.

This bill includes the extension of credits for electricity from renewable resources, carbon sequestration, biodiesel, zero-emission vehicles and more.

Biden's infrastructure plan is accompanied by a proposal to mobilize and incentivize American manufacturing as well.

Spurred by fears that the nation's supply chains are too heavily reliant on foreign countries, which stymied the pandemic response, Biden is eager to revitalize American manufacturing. To this end, he has put forward incentives to reward good corporate actors that reshore

jobs to the U.S. and spur economic development.

The manufacturing communities tax credit is a key part of this initiative — it would provide a 10% credit for revitalizing, renovating or retooling existing or recently closed-down facilities. It would also be available for projects that expand U.S. facilities to grow domestic employment, or for companies that increase manufacturing wages above the pre-COVID-19 baseline of $100,000.

If Democrats bundle infrastructure and manufacturing with climate change, they might push to expand the manufacturing credit to incentivize corporations that hit certain environmental or social benchmarks as a way of furthering the integration of environmental, social and corporate governance factors into corporate performance metrics.

A made-in-America manufacturing initiative is another area for potential bipartisan compromise.

Biden's manufacturing incentives will be paired with policies designed to limit companies moving operations abroad, including:

- A 10% offshoring penalty surtax on services and sales to U.S. customers from a U.S. company's foreign subsidiary;
- A clawback provision to force companies to return public investments, and deny all deductions and expensing write-offs for companies that move jobs overseas, if those jobs could have been offered to Americans;
- Strengthening rules against corporate inversions; and
- Slashing the deduction for foreign-derived intangible income.

As the Biden administration gears up, it is becoming increasingly clear that his international and anti-offshoring agenda are priorities.

Recent announcements of hires to top posts show that the U.S. Department of the Treasury is ramping up for tightening international tax regulations, finding ways to equitably tax multinational companies, and address profits-shifting by multinationals.

Several Treasury Department appointees have also been very critical of the department's regulations on the Tax Cuts and Jobs Act's global intangible low-tax income, on grounds that it provides too many tax planning opportunities.[2]

The Biden administration has also indicated that it will engage on the digital tax debate.

The Organization for Economic Cooperation and Development in 2019 proposed a new tax system that adopted an economic nexus standard, allowing for the taxation of remote sales,

regardless of whether a corporation maintains a physical presence in the taxing jurisdiction.

Earlier this month, at her confirmation hearing, Treasury Secretary Janet Yellen said the U.S. would work with other countries to address international tax rules, including resolving digital tax disputes through the OECD/G-20 process.

In addition to international tax revenue raisers, additional pay-fors could include increases to the corporate income tax rate from 21% to something in the range of 25% to 28%, and rollbacks of various business provisions and incentives for high-income earners in the TCJA.

Biden might also push for new corporate taxes as well, such as his proposal for a 15% minimum book-profits tax for companies with at least $100 million in book profits.

It is unclear whether Biden's incentives and pay-fors will have the desired result.

Investments in green energy, infrastructure and manufacturing will spur the economy and create jobs. Prior to the pandemic, while unemployment was at a low of 3.5%, the employment rate for men ages 25-54 never returned to prerecession rates, according to the Bureau of Labor Statistics.

Additionally, the pandemic has created the lowest female labor-force participation since 1988, according to the National Women's Law Center.

Post-pandemic, the demand for labor will change — trends like automation and a switch to online retail versus brick and mortar will accelerate. Biden's plan purports to create 10 million clean energy jobs alone. However, Biden's green energy and jobs agenda is already caught in a fight between unions and industry.

As green energy industries grow, organized labor has pushed for these jobs to be unionized or at least pay high wages to replace job loss in other energy sectors. Business groups argue that this could jeopardize the success of a nascent renewables industry.

Democratic labor policies will also be problematic for domestic manufacturers. While various manufacturing incentives might spur investments, the sector will also have to incur higher labor costs as a result of Democratic policies.

Additionally, Biden's made-in-America manufacturing policies will also be at odds with the green energy agenda. Reaching carbon emissions benchmarks will be more expensive, without being able to buy more cheaply manufactured foreign products.

These issues are further complicated when viewed in light of the proposed pay-fors. The increase in the corporate rate will reduce some of the efficacy and benefit of the credits, since it will result in the U.S. having a less competitive rate than other developed nations.

If rate increases are paired with a book-profits tax, it could be a double whammy for corporations. Not only will corporations face a new tax, but the book-profits tax limits the ability to offset tax liability credits. This will further reduce the value of some of the TCJA's remaining corporate tax breaks.

Additionally, not allowing other credits to offset tax liability will disincentivize behavior that Democrats wish to promote, such as a reduction in carbon emissions or domestic job creation.

The ongoing pandemic could also jeopardize Biden's proposed tax increases. Several prominent Democrats, including Yellen, have stated that corporate rate increases will not come immediately, until companies have recovered from the effects of the pandemic.

For hard-hit industries, this may not happen until 2022, especially since the American Rescue Plan does nothing to stabilize these businesses. To address this, tax writers might get creative and phase in a corporate tax increase or exempt industries that continue to experience a certain percentage decline in gross receipts.

To further incentivize good corporate actors, Democrats could propose rate-increase exemptions for those that meet certain standards.

Having to water down corporate revenue raisers puts permanence of Biden's individual tax agenda in danger as well. If Democrats are unable to include at least an extension individual tax incentives in the next package, critical workforce supports that Biden campaigned on will no longer be possible. A major plank of the agenda would go unfulfilled leading into 2022 midterms — a risk for Democrats.

4. Full Speed Ahead

Regardless of the obstacles, for the first time since 2010, Democrats have an opportunity to pass a reconciliation bill that includes major legislative priorities.

In 2010, after the passage of the Health Care and Education Reconciliation Act of 2010,[3] Democrats never got another chance to advance priorities through reconciliation.

Learning from the past, the party is now eager to push their agenda through quickly and not squander their slim majority.

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[1] Deficit Reduction Act of 2005, 109 PL 171; Tax Increase Prevention and Reconciliation Act of 2005, 109 PL 222.

[2] Tax Cuts and Jobs Act, 115 PL 97.

[3] Health Care and Education Reconciliation Act of 2010, 111 PL 152.