THE BROOKINGS INSTITUTION

THE TAX CUTS AND JOBS ACT: THE NEW BUSINESS TAX LANDSCAPE

Washington, D.C.

Tuesday, February 13, 2018

Introduction:

GENERAL JOHN ALLEN
President, The Brookings Institution

Featured Speaker:

THE HONORABLE ORRIN HATCH (R-UT)
United States Senate

Moderator:

WILLIAM GALE
Co-Director, Urban-Brookings Tax Policy Center

Introduction to Sessions:

MARK MAZUR
Robert C. Pozen Director, Urban-Brookings Tax Policy Center

Session 1:

LILIAN FAULHABER
Associate Professor of Law, Georgetown Law

BRIAN REARDON
President, S-Corp Association

JOSEPH ROSENBERG
Senior Research Associate, Urban-Brookings Tax Policy Center

Session 2:

ERIC TODER, Moderator
Co-Director, Urban-Brookings Tax Policy Center

PAM OLSON
U.S. Deputy Tax Leader and Washington National Tax Services Practice Leader
PricewaterhouseCoopers

ROSANNE ALTSHULER
Professor of Economics, Rutgers University

ADAM LOONEY
Senior Fellow, Economic Studies
The Brookings Institution

Session 3:

MARK MAZUR, Moderator
Robert C. Pozen Director
Urban-Brookings Tax Policy Center

RICHARD RUBIN
U.S. Tax Policy Reporter
Wall Street Journal

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P R O C E E D I N G S

GENERAL ALLEN: Ladies and gentlemen, good morning to you. It is wonderful to have you here with us this morning, and on behalf of everyone at the Brookings Institution, I am pleased to welcome you to this morning's Urban-Brookings Tax Policy Center Event.

I'm John Allen. I'm the President of Brookings. And it's really great to see you all here this morning.

In a few moments I'll be passing the microphone to the Honorable Senator Orrin Hatch. As Chairman of the Senate Finance Committee, and one of the architects of the recently-enacted Tax Cuts and Jobs Act, Senator Hatch played a major role in moving this ambitious package of reforms through the Committee process and to passage on the Senate floor.

There really is no better person to kick off today's conversation about the dramatic changes this historic legislation will bring to the U.S. economic landscape.

I'm honored to welcome the Senator back to Brookings. I know that we all look forward to his remarks. Senator Hatch, the Senior Senator from the great State of Utah, had a long and illustrious legislative career. A Senator, since 1977, he is currently the longest-serving Republican Senator in our nation's history.

So, I know we are all very eager to begin the substantive portion of today's program; I wanted to take just a moment for us all to thank this great public servant for his many years of service to America. Thank you, Senator. (Applause)

Following his remarks today, and time permitting, the Senator will take a few questions from the audience, and Bill Gale, the Director of the Tax Policy Center, will be moderating the Q&A.

Now, with any other matters to attend to, to include the Senate's consideration of the President's budget submission, we are so grateful that you were able to spend time with us this morning, Chairman. And with that, sir, may I welcome you to

the microphone? (Applause)

THE HON. ORRIN HATCH: Well, I'm grateful to be with all of you here today. This is a great Institution, and I have nothing but respect for you, and if you pay attention to the papers that we bring forth, and a lot of the other things that you've done through the years. And thank you for that kind introduction, and for having me here today.

I'm pleased to have this opportunity to be here at the Tax Policy Center, but I do have to say that I was a bit surprised to get this invitation, after for all it's no secret that the good people here at TPC and I don't always see eye-to-eye on, on Tax Policy. And on a few occasions, during the recent tax reform debate those disagreements became pretty well-known.

Still, at the end of the day, I think TPC actually ended up helping us pass our Tax Reform Bill, and while I may not have always agreed with all of the Center's assessments by the legislation, I very much appreciated the efforts made by some of the leaders here at TPC to correct the record of some of the more outlandish attacks that were being thrown our way.

Make the mistake, abuse of TPC carried quite a bit of weight in this town, and I think throughout the country. Of course I may be just saying all this because in the future I might be looking for a new job. (Laughter) You should all take that into account when you decide how to take my compliments.

But really, even if I may have different views than some of the folks at TPC from time to time, I very much appreciate and respect the work that you all do. And this morning I'm grateful for the gracious invitation to come here and talk about the impact of tax reform, particularly on the business climate here in the United States.

I think the story that I'm here to tell is a good one, but before we talk about the reforms we made to the business tax system, let me just spend a few moments discussing the changes we made on the individual side because that, in my view, is

another good story. In the individual income tax system the new tax law lowered rates across the board with taxpayers and the middle class getting the largest proportional benefit of the tax cuts.

Now, that's something people tend to overlook when they talk about the new law. But opponents tend to only talk about the total dollars in anyone tax cohort, they really talk about system-wide distribution of burden, would shows some pretty interesting matters, and some pretty favorable benefits for middle-class taxpayers.

According to JCT, as a percentage of the taxpayers' income, the largest tax cuts will go to those in the middle and lower-income brackets. First reform, those at the higher end of the income spectrum will see their share of the tax burden go up slightly, but our main goal drafting our tax reform legislation was to provide middle-class tax relief, and by lowering rates and increasing the standard deduction of the child tax credit, we were able, in my opinion, to meet that important goal.

In addition, the new law simplified the tax cut for tens of millions of American families. By nearly doubling the standard deduction we ensure that the vast majority of U.S. taxpayers, more than 9 in 10, will be able to file a simple return without going through the previous maze of deductions and credits.

Now that's an important detail that I hope will not be overlooked as people continue to evaluate the impact of the new statute. Americans pay billions of dollars every year to comply with the tax code and file their returns, the tax reform will and should reduce those costs and help those families.

Now, let's move to the business tax system, which is the focus of today's event. As you all know, our new tax reform law includes a number of significant reforms to the business tax system reform, or I should say, reforms that are already in effect that are paying big dividends for American businesses and their employees.

Chief among the many business tax reforms we enacted is the reduction of the corporate tax rate to 35 percent, which was the highest in the industrialized world,

down to 21 percent, which puts us roughly on par with most of our international trading partners, which I thought was a very good thing. To paraphrase my friend, Joe Biden, this is a Big Fetching Deal. I'm Mormon so I have to use their language. (Laughter)

Prior to the passage of our tax bill, members from both parties worked for years to accomplish this important goal. President Obama outlined a tax plan and it included a significant rate reduction for many corporate businesses. President Clinton, in 2016, was quoted as saying the corporate rate should come down even as his wife's campaign was calling for the rate to go up, which I found quite interesting. I'm not sure they always got along as well as -- well, I'll let it go there.

Former Finance Committee Chairman, Max Baucus, organized support of reducing the corporate rate, the current Senate Minority Leader and the Ranking Member of the Finance Committee both, in the relatively recent past, advocated for bringing down the corporate tax rate.

I know I'm picking on the Democrats right now, but I mention these names, and there are many, many others to demonstrate that the idea to reduce our corporate rate didn't just originate in some Republican fever dream, it was a key objective shared by Republicans and Democrats alike. We've been bipartisan Finance Committee working group reports that show that such is the case.

In fact, prior to last year there were very few people, outside of the Bernie Sanders rally, who honestly argued that our corporate tax rates should not come down. Of course when it came time to produce and pass the Tax Reform Bill some of my colleagues formed, religion, so to speak, in order to decry tax cuts for corporations in our legislation, and argue that American businesses and job creators do not pay their fair share of taxes.

Others argued that reducing the corporate rate would only benefit the corporations themselves, their rich CEOs, and their wealthy shareholders, and I think everyone here would likely acknowledge the problems with that line of thinking. Plans to

reduce the corporate rate were never about catering to one side or the other, but really, like catering to greedy corporations or the decadent rich.

As with the changes to the individual tax system, corporate tax reform has always been about helping middle class workers and their families. That was true when Democrats supported the idea in the past; that was true at the end of last year as Republicans worked to make that idea a reality.

Allow me to demonstrate why that is the case. According to the Joint Committee on Taxation 25 percent of the corporate tax is borne by workers, other economists place that number much higher, as high as 75 percent. Moreover, in just the last 20 years or so, we've seen a massive expansion of pensions and retirement assets, much of which are invested in corporate stocks.

Now, corporate profits have climbed steadily over that period, but with that the retirement plans of middle-class America have expanded as well. In fact, the success of our nation's retirement system has been the largest accumulator of middle-class wealth in history, and the numbers here are astounding.

According to Flow of Funds data compiled by the Federal Reserve, pension assets on the balance sheet of households, and nonprofit organizations have increased from close to $8 trillion towards the end of 1997, to almost $23 trillion toward the end of last year. Now, that's an increase of $15 trillion or nearly 188 percent in 20 years.

In the spring of 2016, a fellow here, that that is from the Tax Policy Center, came before the Senate Finance Committee and testified that about 37 percent of corporate stock ownership was held in retirement plan accounts.

That means that more than one out of every three dollars currently invested in the stock market is held by a pension or retirement plan behind it, and what's more, those numbers have been confirmed by folks at JCT, making the pension and retirement owner category the largest share of overall stock ownership.

No matter how you slice it, by reducing the corporate tax rates we have lowered the tax burden and increases the potential for generating wealth for the American middle class. Like I said, it's a significant shift, and it isn't just a rosy scenario we painted to sell a tax bill. The middle class at stake in corporate tax reform has been demonstrated in spades in the days since the Reform Bill became law.

Over the last several weeks we've seen a stream of businesses come forward to announce that they were awarding bonuses, raising wages, or boosting 401(k) contributions for their employees. According to some estimates more than 340 companies have issued these types of statements, reaching a total of about 3.5 million workers.

I'm not going through the whole list, but let's highlight a few. Last week U-Haul announced that all of its full-time employees would be getting $1,200 in bonuses, with part-time employees getting $500. Also told more than 28,000 U-Haul employees will be receiving bonuses providing them with around $23 million in benefits.

The very same day, Tyson Foods announced that 100,000 full of part-time employees would be getting bonuses of $1,000 and $500.

Then last month, Walt Disney Company announced that, as a result of the new tax cut it would be issuing $1,000 cash bonuses for 125,000 employees, $125 million in total as well, that's another $50-million investment in employee education programs.

And it doesn't end there. As just one more example, Waste Management is providing $2,000 bonuses for every North American employee not on a bonus or sales incentive plan, which specifically includes all hourly and other employees. Now, that's $2,000 to approximately 34,000 middle-class employees.

Some of the naysayers out there, and there are a few, if you believe it, complain that these bonuses and benefits are not significant. I say, tell that to workers and families on the receiving end of these new benefits. For a middle-class family $1,000

is three or four car payments, a couple months' worth of groceries, or rent, or mortgage payments.

And, as the economy continues to expand American workers will continue to benefit, as well as the companies that employ them. In the coming months and years we are likely to see more investment and more jobs created here at home, which means better paychecks and more opportunities for our nation's families.

While all of this news has been getting the attention, the international business tax reforms to be put in place in that legislation, and have in some respects flown under the radar. But don't get me wrong, people have known they were there, but they are just not starting to get the attention they deserve.

The new tax law converted the U.S. tax system away from a worldwide system and toward a territorial one. By itself this shift would be a major step towards modernizing our tax system and encouraging more expansions and investment in the United States.

Of course, this isn't the only international tax reform put into place. We also established measures to prevent the erosion of our tax base in order to make sure invested capital in our tax base remain here at home instead of being shipped overseas from a U.S. company to a foreign entity.

The Base Erosion Anti-Abuse Tax, or BEAT, places limits on the extent to which U.S. companies can deduct interest and royalty payments to parent companies offshore. The provision was drafted with an eye toward preventing the type of transactions that were all too common in the years before the recent tax reform efforts. For years we saw the wave of inversions as American companies opted to move their legal headquarters offshore in order to, among other things, escape obnoxiously with high corporate tax rates, and our corporate worldwide tax systems.

The clincher, in many cases, was the fact that our system would allow a foreign parent company to engage in earnings stripping and other forms of tax avoidance.

Both parties saw this is a problem, and with our new law we were able to effectively address it without draconian regulations, or punitive governing rules. Between a reduced corporate rate, the transition to a territorial system, and the BEAT, we have created a system that will help prevent inversions, earnings stripping, and other forms of tax erosion to keep investments in the United States from being shipped overseas.

We are getting good signs on the effectiveness of this approach as well. Just yesterday *The Wall Street Journal* reported that under the new law a significant number of companies that inverted over the last few years will see their taxes go up at least slightly. This is what it means to be competitive with the rest of world. This is what it means to operate in the 21st Century.

It is truly a shame that we allowed our country to become less desirable -- a less desirable place to do business, than so many of our trading partners. Fortunately, our effort to fix this problem took some big steps forward with the passage of our Tax Reform Bill.

Of course none of this will matter if it's not all properly implemented. That's why we will keep the pressure on the administration to do things properly, and as Congress intended. I'm going to keep working to ensure that everyone that recognizes and respects Congress's role in this process. Where things are, potentially, unclear in the law Congress should be the one to determine and explain what was intended. I will continue to pursue facilitating this type of consistent interaction as things move forward.

There are other things to discuss, like the important role of pass-through businesses for which we created a new deduction to allow smaller businesses that are taxed at the owner level, to better compete; to better compete with those in larger corporations. This provision is key and deserves more discussion.

However, for now let me just say that I appreciate all the work done by TPC and others here today. You've been very helpful, and I look forward to working and, in some cases, debating these issues with all of you going forward.

With that, I want to thank all of you for being here today. I also want to, once again, thank the Tax Policy Center for inviting me to speak. I appreciate the invitation, and I want to thank you, and God bless you all. Thanks a lot. (Applause)

MR. GALE: All right. Thank you Senator Hatch. I'm Bill Gale, Co-Director of the Tax Policy Center. We are extremely short on time, so I will pass on the Moderator's prerogative to ask questions. And I think we have time for two questions. So, let's see, yes, to the right. And, Joey, let's set up the second one, too.

QUESTIONER: Thank you very much. Larry Chacker from Chacker Communications. With all due respect, Senator, you focused a lot of your attention on bonuses that companies have given out, and granted 1,000 or $2,000 is not small change, but it's not a game changer, and the reason these corporations love to give bonuses is because it's not attached to benefits.

MR. GALE: I forgot to add, please keep your questions short, and to make sure it's a question.

QUESTIONER: So, is this truly going to help middle-class folks? Thank you.

THE HON. ORRIN HATCH: Well, I think it does help middle-class folks. The question in my mind, is about that but, you know, we could have done this in other ways, we can, you know, have more, you know, money for the competition. There are a number of things we could have done, but I think -- I think we did a pretty good job under the circumstances, and most people who I talk with, agree.

MR. GALE: Thank you. One last question. Yes?

QUESTIONER: Working on the premise that there's nothing perfect in this world, if you had the chance, what would you change about this law? Can you comment on it at this point?

THE HON. ORRIN HATCH: I'm sorry. What would I change about what?

QUESTIONER: The tax law.

MR. GALE: The tax law. How would you make it more perfect? (Laughter)

THE HON. ORRIN HATCH: Let me just say this, I can make some changes before I leave here, I mean, before I leave the Senate, but there are a lot of things that we wish we could have done. Let's face it, our tax code has been -- it has been less than satisfactory for a number of years. I think we did pretty well under the circumstances, especially when bringing both sides together.

I've been able to do that as Chairman of the Finance Committee, although there was a desire not to come together on a number of occasions. So, I think, you know, we just have to go into the future, and hopefully we can do some things that will make this tax code even better than it is now.

And I think we made some pretty big strides here, and I think even my Democratic colleagues are pretty happy with what we did, and Republicans are not as happy as they would like to be, but that's always the case.

MR. GALE: All right. Let me thank you, Senator Hatch, for coming over here, I know you have an incredible busy day with immigration and this thing called the budget that just came out, and so on. So, thank you again for visiting with us, and sharing your thoughts, and we greatly appreciate that.

THE HON. ORRIN HATCH: Well, thank you all for being here. And thank you for the work that you do, and thanks for the intelligence that you continually give us up there in Congress. We couldn’t run the place without good people like you. So, I'm very grateful to you, and I'm very happy to be here. And I hope this session wasn’t too boring for you. (Laughter)

MR. GALE: Not at all. Thank you very much. (Applause)

SESSION 1

MR. GALE: All right. We have to adjust the schedule slightly to make it

work for Senator Hatch. We thank Senator Hatch for being here. We appreciate all of you coming here. I'd like to welcome everyone to the *Tax Policy Center Event*.

Our topic today is, indeed: *The Recent Tax Overhaul*. I use those words advisedly. We are going to call it *The Tax Cuts and Jobs Act*. We are fully aware that that is not the official name. I don't know what the official name is, but you can read about in our legislative record, and we thought calling it The Tax Cut -- or formerly known as the Tax Cuts and Job Act, would also not be very efficient, so we are just going to call it Tax Cuts and Job Act.

From our perspective, as tax analysts it's the gift that keeps on giving. We had a conference a couple of weeks ago on the impact of the Tax Act on states; that was held at the Urban Institute, and you can find it online.

Today we are going to talk about the business side of things, two of the most innovative sets of changes in the Tax Reform Act occurred on the business side, I don't mean that cutting the corporate rate that that's a big change, but that's sort of a standard change keeping the -- simply adjusting the rate. I'm talking about the changes in the taxation of pass-through businesses, and the effects on multinational firms in the treatment of foreign versus domestic source income.

After that we'll have a conversation with Richard Rubin. So, we are going to pack a lot in this morning, and I think it should be a lot to say, I was going to say that I was going to turn the podium over to Alexandra Thornton of CAP, but I'm not going to do that. She is not here, she's not feeling well.

So, I'm going to continue on as Moderator of the first session on pass-throughs, with Lilian Faulhaber at Georgetown; Brian Reardon from the S-Corporation Association; and Joe Rosenberg from the Tax Policy Center.

So, if you guys will come up, we'll get ready for the first session. All right, so we have a lawyer, an economist and a practitioner. And we will start in that order.

Lilian, without breaking our minds; please give us a legal overview of

some facts and figures.

MS. FAULHABER: Great. Thank you. So, as of now the tax benefit that was applied to pass-throughs, was not a special rate, per se. Instead, it was the fact that they were not tapped at the entity level, and so they didn't have the double taxation of C corporations.

But as Senator Hatch mentioned, tax reform effectively added a whole new rate that applies just to pass-throughs that earn certain types of business income. So, tax reform added Section 199A which provided 20 percent deduction for these types of businesses, income earned through a pass-through.

So, with the top rate of 37 percent that applies to individuals now, this means that pass-through -- the individuals that earn income through a pass-through and it's this type of business income, had a top effective rate of 29.6 percent.

Now, one thing to know, while this is a noticeable drop from the top individual rate of last year, the corporate rate also dropped down to 21 percent, which is still below this 29.6 percent, so the relative appeal of pass-throughs, it still remains to be seen relative to corporations.

But to understand who gets the 29.6 percent rate, need to know some terminology that's in Section 199A. So, the only income that qualifies under Section 199A is qualifying business income earned by a qualifying trade or business.

So, what is a qualifying trade or business? A qualifying trade or business is any trade or business other than the following two categories. So, the first employees: if you are an employee, if your trade or business is working for someone else as an employee you do not benefit from Section 199 capital A.

The second category is being a specified service trade or business that includes investing or investment management, health, law, accounting, athletics, financial services, or any trade or business where the principal asset is the reputation or skill of the employees. So, this means that the more tied your skills or reputation, are to your

business, the less likely you are to benefit from 199A, to simplify that.

Now, note the qualities of excluded industries, there is an exception if your income is below $207,500, you end up benefiting, at least in part, from 199A, once you go above that threshold for a single individual, or double that threshold, then if you are in the specified service industries you can't benefit at all.

So what do those specifics mean? Those specifics mean that you definitely have benefit if your trade or business is being an employee.

If, however, you're an independent contractor, or business owner, or somebody who falls outside of being an employee, then the question is whether or not you are in that specified trade or business. If you are in those specified trades or business, you also can benefit, unless your income is under the cutoff.

So, what kinds of incentives are built into this definition of a qualified trade or business? Well, shifting away from being an employee, recharacterizing into being an independent contractor, or some other non-employee business owner. That's not necessarily as easy as it sounds, there's still the 20 Factor Test to determine whether or not someone is an employee or an independent contractor, and this also, from a legal perspective, has other consequences beyond just taxes.

It has consequences in terms of liability, it has consequences in terms of workers comp, and on the tax side it has consequences in terms of Social Security, and Medicare, and other types of taxes.

Now, if you're not an employee, this also creates an incentive to shift away from being in those service sectors and to recharacterize your business. So, either recharacterize your business as owning real estate, or engaging in some other type of activity, or separating out the aspects of your business that are linked with those -- those non-approved service sectors and, instead, focusing more on the other types of businesses that you provide.

Or, you could do the opposite. Since the focus of 199A is whether or not

your reputation or skills are the principal assets of your business, you can try to add more -- more qualifying activities to make sure that your reputation in skills are no longer the principal assets of your business, they are only a minor part of your business. So, those are some of the incentives underlying the definition of the qualifying trade or business.

The next question is: even if you have a qualified trade or business you can only benefit from the 20 percent deduction if you have qualified business income. So, what is qualified business income? Qualified business income is 199A, is the very section of your provision is everything except the following things. And the following things are capital gains, so various types of passive income, and a reasonable compensation both to employees, and to getting the form of guaranteed payments to partners.

So, essentially qualifying income doesn't include passive investment income, and it doesn't include reasonable compensation. So, this essentially says that if you look at what counts as a qualifying trade or business, qualifying trade or businesses, are trade or businesses that are more leaning on the passive side, but the income itself that qualifies is more of the active income than ends qualifying within those businesses.

Now, over all of that, there are other umbrella limitations. So, the 20 percent deduction can be no greater than 20 percent of your taxable income. So, if everything you earn is qualifying business income, then you probably won't get to have a full 20 percent deduction of that because it will be limited to your taxable income after you’ve taken out all of your other deductions.

There's also a limitation on the deduction based on how many W-2 wages you pay, or the amount of depreciable property that you own. So, if you don't pay out any W-2 wages, and you don't have any depreciable property -- depreciable assets you can't benefit. But as long as you have one of those you will be able to benefit from 199A, up to a certain point.

And then one other limitation that is worth noting, is that because this is

seen as an individual provision, it expires after 2025, so this is a new way of dealing with a pass-through that has a short period of time when it is scheduled to exist.

So where does this leave us? This means that certain taxpayers just can't benefit. C corporations, by definition, can't benefit, employees can't benefit, and partners or members and past-throughs whose income is based on reputation investment, or other services like law or medicine. And even those who can are limited based on things like W-2 wages and depreciable property, and the type of income they earn.

But this still creates this whole new benefit for the types of pass-throughs that can benefit. And as shown by Kansas, where we had a full exemption base for income earned from pass-throughs, this can create changes in behavior, and this creates distortion.

So, I was asked to end my presentation with some questions, so I will ask -- I will frame my questions in two ways. First, like my first question is in the category of why, and the second question is the category of: what are the effects?

So, on the "why" front, we already have a huge number of pass-throughs in the United States. As we all know, since the 1980s the number of pass-throughs has dramatically increased, the amount of business income earned through pass-throughs is now in the significant majority. And so one question is: do we need to have a special 29.6 percent rate for pass-throughs?

What is the incentive -- was the reason for this to reward those companies that had already become pass-throughs, or those individuals who were earning income through pass-throughs? Or, was it to create an incentive for even more pass-throughs than we already have?

And the second set of questions, in terms of the effect, I think you can break into two parts. So, first what are you going to be the effect on existing employees? Will any of them switch to being partners or members of pass-throughs as has happened

in Kansas?

Now, as some of my colleagues, some academics, Diane and Sheila, pointed out, that's not as easy as it looks, there are all those other illegal limitations that I mentioned, and there are so many employees already being shifted to independent contractor status in the today's economy, it's worth when questioning whether or not this will change the number of employees who are being shifted into them into independent contractor status.

But then the second part of this question about the effect, is thinking about whether or not there are going to be C corporations that will respond? Will C corporations shift to pass-through status? Or will the 21 percent corporate rate be enough to prevent that type of change.

So, I will leave it with those questions, and hand it over to my other panelists. And I look forward to the discussion.

MR. GALE: All right. Thank you. Before I turn it over to Joe, I was remiss not to mention that if you are following online, we welcome you this morning, and you can tweet or otherwise communicate under the hashtag, BusinessTax.

So, Joe, over to you.

MR. ROSENBERG: Thanks, Bill. So, that was a terrific summary of Section 199A, giving us the official title, that Lily gave. As you can get a sense, it's very clear. I assume there are no more questions. (Laughter)

What I would, sort of, like to do is take a little bit of a step back. I think what Lily made clear is, there's a lot to this special pass-through deduction. My view is, there's still a lot to be learned about how it will be interpreted, how Treasury and IRS will administer and enforce it.

So, what I'd like to do is sort of fast-forward a couple of years, and think about how we will view this pass-through deduction in a sort of hindsight, and then how we should evaluate it in terms of whether it's good policy or not.

And to sort of, my take on this is for a best-case scenario, is it's a large new tax expenditure with sort of dubious policy merit. And that's sort of the good case, there's also the rest that it's sort of balloons, and that it really proves to me unadministerable, and unenforceable, and it could, in fact, be much worse and more of a threat to our individual income tax system.

One of the ways we often engage tax policies is through some common metrics of fairness, efficiency, simplicity. So, how should we think about this pass-through deduction? In terms of fairness, or who benefits, we have a fairly good handle on who currently reports pass-through income.

So, currently about 85 percent of net income from pass-throughs is reported by the top 20 percent of taxpayers, more than 50 percent of that, by the top 1 percent of taxpayers, in terms of annual income. In the case of partnerships and S corporations that's more like 70 percent of net income or of the top 1 percent.

So while this deduction will benefit, some benefit to a large number of taxpayers, lower and middle-income taxpayers that they report pass-through income, TPC's analysis suggests that about 50 percent of the benefit are from this pass-through deduction will accrue to the top 1 percent of taxpayers. So, this little question, just in terms of who reports pass-through income that the majority of the benefit will go to higher-income taxpayers.

In addition, it will treat taxpayers with similar incomes very differently. So, again TPC's analysis found that the average tax cut for someone who primarily earns pass-through income would be about three times the size of the average tax cut of a wager. So, it sort of doesn't advance the so called horizontal equity of tax.

Now, one question is: are you willing to sacrifice something on the equity dimension for gains along other dimensions, like efficiency? Will the pass-through deduction encourage pass-through businesses to hire more, invest more, and grow the economy?

Here, my view is that probably it's positive, yet modest. So, you should expect lowering the rate of profit's tax might reduce the cost of capital and increase firms to invest a little bit more. But there are far more effective means that in fact the Tax Cuts and Job Act implemented alongside this, including expanding Section 179, expensing for small businesses, and significantly increasing bonus depreciation to 100 percent, at least for five years.

So, there are probably some gains along the efficiency dimension, but those should be weighed against other costs. Again within the sort of area of efficiency and, in particular, I think as Lily, sort of, again made clear, it really does treat a lot of businesses differently.

And so, you know, we probably won't get into the full discussion, and frankly I think a lot is still to be discovered, but I think Section 199A or the pass-through deduction will create a lot of new distortions, exacerbate a lot of distortions related to entity choice, how businesses organize.

Do they remain as the pass-through entity, do they try to convert to a corporation, or somewhere in between? You know, the last sort of dimension is simplicity, and I won't spend a whole lot of time belaboring this. I don't think there's a case that this improves on the simplicity of it.

So, lest you think I'm too pessimistic, or harsh on this provision, remember that's my sort of optimistic case, (laughter) that this sort of -- the so-called guardrails hold. According to JCT, this provision, the annual cost of about $50 billion, so post the Tax Cuts and Job Act that will be a very large individual income tax expenditure, certainly a top ten individual income tax expenditure, if not top five.

And I think there's a real concern that these rules, and these lines that are drawn prove to be quite hard to enforce, and that there's considerable opportunities to game this provision, especially by, you know, taxpayers with the highest pays, and the most talented lawyers.

And so, again, just as a sort of frame of reference, TPC, sort of, did a hypothetical of: what if there were no guardrails in the provision, so, just a straight 20 percent deduction on all pass-through income? That would increase the cost of the provision by at least 50 percent, so you'd be talking about a $75 billion a year cost. So, just to give you some sense of what --

Yeah, I sort of viewed that JCT scored 50 billion a year is a relatively conservative estimate, sort of assumes guardrails worked and IRS an important --

So, you know I have no doubt that my lawyer and accountant friends will come up with, you know, a 1001 ways to sort of game the system, or however you want to phrase it, you know, help their clients take advantage of this provision.

I don't exactly know how that will play out, I assume there will be some sort of cat-and-mouse game between taxpayers, and Treasury, and the IRS. What I do know is there's a large body of economic evidence that suggests that taxpayers will respond to tax rate differentials in how they report their income.

So, it's not a question of whether the pass-through deduction will encourage taxpayers and businesses to shuffle their affairs to take advantage of the lower rate, but it's really a question of magnitude, and whether it's sort of -- or manageable tax expenditure, again on the order of $50 billion a year, or whether it's much worse than that. And again, I think really becomes a threat to the individual income tax system.

So, I will probably stop there. And I think to answer one of Lily's questions. I mean I think the pass-through deduction was really a solution in search of a problem. It was really more about solving a political problem which is: how do you lower the corporate rate while doing something for pass-through businesses, so they support the legislation? Rather than, you know, an economic case that says, you know, this is based on a real need from either equity efficiency, or simplicity argument of the real economic base. I'll stop there.

MR. GALE: All right. Thank you. Brian.

MR. REARDON: Thank you, Bill. I'm Brian Reardon, with the S-Corp Association. I think I'll start like Joe, start at a high level, and work my way down. Personally, I would like to talk a little bit about sort of the value proposition of pass-throughs in general. I think they get plenty of short shrift in the tax community. The second I'll talk about the tax bill that just got passed, and the implications for S corps specifically, and pass-throughs in general.

And then talk a little bit about where we see things going. As you can imagine, we are an advocacy organization, so our job right now is to figure out, where do we go with the rules that are in front of us.

In terms of the pass-through value proposition, you know, I think if we were to start with a blank sheet of paper and say: how are you going to tax businesses moving forward without any pre-existing rules? Many people that we -- certainly a plurality, and maybe a majority in tax people both the left and right, would agree that the pass-through structure, the way the S corps are taxed, is the correct way to tax business income.

You tax it once, you tax it when it's earned, you tax it hopefully at a reasonable rate, and then that's it, and you avoid that double tax that the C corps have to pay that creates all sorts of distortions in the economy, and frankly, I think that the bill that we just passed is going to increase those distortions.

What we did with the bill that just passed is lower the rate at the C corps suite, the C suite, but we sort of relatively increased the penalty for kicking that money out to your shareholders. So, you increase the bias towards keeping the money within the corporate structure, which could lead to tax sheltering in many cases, and less about doing something, you know, making decisions based on what's best for your shareholders, for the economy.

With S corps you sidestep all that, you don't have that second layer of

tax. Moreover, when you do earn money it's taxed at the shareholder's progressive rate. So, if you have shareholders of low income they pay a low rate, if you have a shareholder who is high income, they pay a higher rate. It's much more progressive, it's much more accurate relative to, if we want to progress a tax code S corps embrace it. C corps don't necessarily do that.

A financier would say -- you know, Joe was talking about who pays taxes, and all that sort of stuff. Actually what he said was: who is going to save money? The conversation of, who actually pays the taxes rarely gets talked about.

You know, to jump ahead and answer one of Lilian's questions. There's no doubt in my mind that what's going to happen under this tax bill, is more and more economic activity is going to shift out of the pass-through world and back into the C Corp world, which means you are shifting income out of what's properly taxed into the double tax that creates most of the distortions that hurts the economy in the first place.

That's not a good result. It also means that the income inequality that Joe is talking about is not going to disappear. It's not like large S corps of people that I represent are suddenly no longer going to own the business, this is going on as the C corps. So, that income is no longer going to show up on their income taxes, so it's no longer going to get a show up on the income inequality fence. This is something that's been written about quite a bit, and it's not necessarily a good thing.

So, that's the big value proposition. Keep in mind, when we talk about: Why should we get a deduction? Why should pass-throughs have been part of the discussion in the first place? Over 50 percent of American people, private-sector workers, get up every day and go to work at a pass-through, 57 percent of them. So, when you're talking about what's good for the economy, what's good for Main Street, that's a big part of the issue, and pass-throughs have to be part of the discussion.

Moreover, the businesses I represent are literally Main Street businesses. They are out there in the flyover country, and I think there's a value, there's

an importance to having economic decision-making spread around the country, and not just housed in New York, and Chicago, and San Francisco.

Having people make decisions about hiring investment who actually live in the communities where those decisions are being made and going to have an effect, is really important. And I think during the financial crisis we saw the importance of that.

My guys didn’t go belly-up. My guys didn't over leverage. It wasn't my guys who created the financial crisis. My guys helped to be the safety net to stop it, and to prevent it from being worse. So, that's the value proposition that I'm talking about.

The tax bill: I found it interesting that that Lilian spent the entire time talking about the deduction, right, as you should have, because it's really complicated. Yeah? I mean my guys are still trying to figure out what it all means. We spent no time at all talking about the complexities of the 21 percent corporate rate, right? How much time could you spend on that? Not much, it's 21 percent, right. You make money as a C corp you pay 21 percent. Right?

How much do you pay if you're an S corp? Is it 29.6? Is it 37? Is it more? The way they've structured the deduction is that you get the 29.6 if you're in the right industry, if you make the right amount of money, if the location where you earn the money is domestic and not international.

There are other complicating factors that we haven't talked about. We spend a lot of time during the debate over the tax bill talking about the state local tax deduction. Right? C corps continued to be able to deduct that as a legitimate business expense.

During the debate there was a high degree of confusion over whether S corps can continue to deduct the state local tax, rather than income taxes. Raise your hands if you think S corps can continue to deduct the SALT. Raise your hands if you don't think that they can? Everybody is going to raise their hand.

It's complicated, as with everything in this bill about pass-throughs. The

simple -- where we ended up was, if the entity, the S corp itself pays the tax. So if it's property tax, if it's a sales tax, if you're in one of those states where they actually have an entity-level tax, or disregard S corp elections, then yes, you can continue to deduct the state and local income tax.

If you are in a state that doesn't, and there's the preponderance of those states don't -- I'm sorry -- do not tax at the entity level, the tax flows through to the shareholder, then you're not going to be able to deduct those taxes.

So, if you think about it, California the top rate there is 12, 13 percent, at a 30, 37 percent rate, you're talking about 2 or 3 effective percentage points more that S corps are going to pay just to be located in California to do business in California versus, say, if they do business in Texas, or Wyoming, or in Florida where they don't have an income tax. It's a huge variation, and it's going to cause problems. It's going to distort behavior.

People are going to move out of California and into Texas and some other places. The NIT, the NIIT, the ObamaCare tax, right, it applies to S corps but only if you don't actively participate at the business. So, if you are a passive shareholder in an S corp, like you'll be a passive shareholder in a C corps, you’ve got to pay that 3.8 percent tax. If you materially participate, you work at the S corp, you don't have to pay that 3.8 percent tax.

So, again, you've got a differential based on whether you're active or inactive. So, the net result is that some of my members will get a 29 percent -- a 29.6 percent rate, but only if they are in a state without an income tax that flows through the shareholders; only if they actually materially participate in the business, only if they have enough employment, only if they have enough investment. Only if -- if they only have domestic income, because international income doesn't qualify for the deduction. It's very, very complicated.

Add to that fact that it's all temporary. It goes away. So, I have been

talking to every single one of my members over the last month or so, and every conversation starts with: so what are you going to do? Are you going to be an S corp? You're going to be a C corp?

Every one of them is running the numbers, and every one of them doesn't really know. Some of them -- one of my guys said, you know, it's 80 percent 90 percent chance we are going to be a C corp next year. And some of our guys are like 100 percent we are going to stay S corp.

The two main factors appear to be, one, how much of your dividends, or how much of your earnings do you have to kick out to your shareholders? Are you in growth mode? Or, are you actually spinning off money to your shareholders?

And then something I didn't even talk about is, the that if you put everybody in the C corp world, public companies who can reward their shareholders through the price of the stock, and the fact that they can sell it on the markets way over here where the C suite guys don't even know that transaction took place, have a huge advantage over closely-held C corps, because closely-held C corps, don't have the ability to sell stocks to reward the shareholders. They have to kick out money to their shareholders.

So, if you're a C corp, you retain all your earnings, you'd get to retain 79 cents on the dollar, if you're and S corp, then you have to kick out money to your shareholders so that they can actually be rewarded for owning a business, because otherwise they are not going to get anything out of being an owner of the closely-held C corp, right?

If you're in that situation, you are having to drain money out of the business. It's not a level playing field, that's why S corps were created in the first place. So, going back to the decision tree, my guys, if they are kicking out dividends they're more likely to remain in S corp. If they think about selling the business, if there's a potential for a sale, five years, ten years down the road, they are more likely to remain in

S corp.

Well, if they are in growth mode, and there's no intention to sell the business, they are likely to be a C corp next year. You're going to see a lot of activity moving from the pass-through world to the C corp world under this bill.

So, that's kind of the landscape. And what are we up to? As Lilian and Joe made clear, the deduction itself is remarkably complex. It doesn't put my guys on a level playing field. Again, you know, C corps, if they want to convert they can pay 21 cents on the dollar. At best, my guys are paying 30 cents on the dollar, that's not level.

And then if they have to distribute out even more money to keep their folks happy, they are retaining what, 60 cents, 50 cents, 40 cents on the dollar. That's not going to be a level playing field. And so one of our goals is to make the deduction as robust and as clean as possible, and there are so many technical details, it's hard to start.

One is where you calculate the deduction. So, for instance, if you just have a single S corp, all your business is located there, then it's fairly straightforward, right? What happens if you have multiple entities, and you have losses here and gains there?

One of my guys, a manufacturer, has multiple entities, it has nothing to do with taxes, it has everything to do with administrative ease and running the business. So, they literally have one LLC sitting over here, and he has all their payroll, all their insurance, their line of credit goes through that LLC, there's no money going in that LLC. The LLC doesn't actually have any operations, it just houses all the administrative costs of the business.

So they only have one payroll vendor, they only need one line of credit, that's simpler, right? Well, with the deduction all the employment is over there, and since the deduction is limited to 50 percent of payroll, Dan is not going to get the deduction unless he completely reorganizes his business, if you calculate it at an entity-by-entity

level, or if you calculate it at the trade or business level.

So, one of our goals is to allow grouping, like they allow right now under 469, so that businesses can take and groups their businesses in a way that makes sense, and then they can get the deduction that they're owed. And the beauty of that is that because the guardrails, you know, 50 percent of your W-2 there is a hard stop to how much of a deduction they could actually get. It's going to be 50 percent of your W-2. So, there really isn't that opportunity for gaming.

And I'll say one last thing in response to something Joe said, and actually Lilian too. There are going to be opportunities for gaming under this bill that I think we support shutting down, I think everybody in this room supports shutting down, but you have to distinguish between the rules that don't apply to people making less than $315,000 a year, and the rules to apply with everybody else.

Because the rules that apply to everybody else, I don't think they are perfect, but they're pretty good. I mean there is a certain justice to the wage limit, it means that if you want to get the deduction you have to go out and actually create some jobs. We can live with that, the challenge is that there's going to be so much attention focused on what's going on with the people under 315,0000 that I think it's going to undermine the value, or the legitimacy, or the perceived legitimacy of the deduction in total. So, that's one of our challenges.

The second thing is, state and local tax deduction, we are working both at the federal level and the state level to see, and make sure that S corps can continue to deduct that as a legitimate business expense. It's going to be an uphill battle, but I think we can make some traction there.

And then I had one last thing to talk about. Oh, yeah. And then just -- excuse me -- simply put, strengthen and make permanent the deduction. My guys can't plan under the current circumstances. All right? If you are in growth mode, and you are trying to figure out: am I S, am I C? What do I do here?

Right now under the bill you can expense your CapEx, right, five years of expensing, that's great, but if you're an S corp what that means is you are taking income now, creating a loss through your expenses, through your CapEx, and taking the expensing, and you're pushing it out in the out years when the deduction doesn't exist. So, you would be taking the deduction now when the rates are low, and pushing it out in the future when rates are high. Well, that's not good. We've got to figure something out there too.

So finally, the last thing is making the deduction permanent. You know, as Joe and Lilian said, the deduction itself is very complicated, it's going to be difficult to work through but, you know, we are committed to trying to make it as clean as possible, make it workable for real businesses with real profits, and real employees, and real investment, the people I represent. And hopefully, we can get there.

MR. GALE: Right. Thank you, all. So, as a listener we get that it's complicated, and there are inequities. I want to build on Lily's questions at the end, Joe's comment that the provisions are a solution in search of a problem, and your comment at the end that there is some logic to it, in terms of, you have to have the wage deduction.

So, my question is just, we can all be critical of the provisions, but just sort of step back, give a charitable -- like a charitable interpretation, put on your tax cut advocate hat and answer: Is there an underlying logic to the provisions? Yes, they are messy, but is there some broad consistent goal that they're pursuing? Is it creating jobs? Is it keeping businesses in the U.S.? Is it affecting -- keeping people in one corporate form or in others? Can you see any method in the madness?

And let me start with you, Lily, since you knew all the provisions.

MS. FAULHABER: Can I see any method in the madness? Let me let me go through your options. I don't actually think you can argue that it's encouraging paying the wages because of the depreciable asset addition. So, it used to be -- in an earlier version it used to say that you couldn't get this unless you were paying out W-2

wages, but now you can get it if you have some depreciable assets, so, I think the addition of that.

There are reasons to have that, but it's not -- it moves this away from pure encouraging of paying out wages. I think that if you step back and you take a sort of bigger picture, I can see the argument that if you're going to reduce the corporate rate you also want to have a lower rate that applies to pass-throughs.

I can understand that and I can see that logic. I think that the specific guardrails, because of the different ways that they're pushing, I don't see one overall logic. And what I mean by that is that by excluding certain types of industries, or favoring some industries, disfavoring other industries, but then focusing on certain types of income within those industries, I feel as if that's a little -- that's sort of all over the map, and it doesn't seem to have one clear message.

I would love to hear if you think that there is a clear message there, that there's a reason to be favoring the industry it is favoring, and disfavoring the ones that it's not, because I think that a lot of the guardrails have to do with trying to prevent the shifting of employees, of wage-earning employees into partnerships. I think that's an overall limitation, but I'm not sure that that's a method to the madness.

MR. GALE: Joe, what is the best possible case you can make for the pass-through provisions?

MR. ROSENBERG: I think Brian and I agree on a lot, I think all three of us agree on quite a bit. I mean I do think a lot of it stems from the pressure that the low corporate rate presents, and I don't know if this counts as an optimistic or charitable take on the provision, but I mean, it could have been worse. (Laughter)

So, I mean look at -- I mean the House version of the pass-through deduction, it wasn't even a deduction. You know, it started out as a cap on the rate, so would really only benefit higher income people, and it turned on a sort of, in my view, completely sort of not meaningful -- or lessen, it's an extremely meaningful distinction

between active and non-active or passive.

So, I mean I do agree that the wage limit is one of the better guardrails they could have come up with, as you said. I mean it actually requires some employees that you're actually paying wages to. You know, but in terms -- I mean it's certainly the case that this is going to affect different companies differently. So, this is not -- you know this is not providing the sort of neutral treatment across entity type.

But, you know, I mean in terms of sort of level playing field, you know, you do have to keep in mind that there is that second layer of tax on corporations, so even with a 21 percent corporate tax rate, if profits are fully distributed and subject to a top capital gains rate or a dividend rate of 23.8, you're looking at an all-in 40 percent rate just on immediately distributed corporate income anyway.

So, you know, again I'm not all that optimistic that there's tremendous, you know, real investment and hiring gains that will result from it.

MR. GALE: Great. Brian what's the best case?

MR. REARDON: A couple things. One, you know, Joe correctly points out; there is the second layer of tax you have to calculate the effective rate of that. I would point out that very few dollars that are earned by a C corp are immediately kicked out to fully taxable shareholders. In circumstances like that, that business has figured out how to be an S corp because you can't really compete as a C corp under those circumstances unless you're a utility, or heavily regulated, or in a particular industry.

In terms of sort of the value of the deduction, I think a couple things. One, we would have preferred a rate, obviously, I think the challenge with the deduction is that it does have a tendency to be limited, it's seen as a tax expenditure, as a special provision, as opposed to a rate which is seen as the rate, right; and so you see in this bill examples of that, so many different rules.

As Lilian and pointed out, you have the specified service companies and the limitation on them. As soon as you create a separate rate for pass-throughs, then

you have to have guardrails, and the challenge is how do you go about making those guardrails, so you distinguish between real business profits, the things my guys make, and the Newt Gingrich and the John Edwardses of the world who create, you know, an S Corp and use it to block paying, at that case, payroll taxes, in this case to try to get the deduction.

It's not easy, it's something we've struggled with since 1993, and we came up with a lot of ideas. Some aspects of them were embraced, others were not, but I do think that, you know, as soon as you go down that path it just creates problems. And what we are seeing here with the complexity of this rule is that it's going to be able to -- I think there's going to be a long period of falling out where the rules are refined and clarified.

I think we could have come up with better guardrails, I think some of the guardrails like the 50 percent limitation on wages, it's workable, there's a certain justice to it. Limiting businesses based on what industry they are is problematic. I think, politically, they didn't want lawyers, and hedge funds, and folks to get it, but there are law firms that create a lot of jobs. And so what's the difference between a job at a law firm and a job at one of my members who is a manufacturer?

It's kind of hard to distinguish it on an economic basis, on a sort of relative value basis. So, as soon as we went down that road it's problematic. But we did go down that road, and certainly my task in the next few months is to help make the rules as clear and workable as possible.

MR. GALE: All right. Thank you. We are running really sort of time, but let's take two questions. Bob?

QUESTIONER: So, I'm trying to figure out, Joe, who exactly is getting this deduction in the top percent. If they are in all the identified service industries, if they are making 400 or more, they are not going to get it, and also if they are just -- if they don't have much W-2 income they are not going to get it. So, I'm trying to figure out --

and passive owners aren't going to get it -- so is it active owners of real estate, oil and gas and manufacturing? I mean who is getting all this benefit? I'm trying to think about, practically, who is getting it.

MR. ROSENBERG: So, I don't think there's a limit on -- I don't think the deduction is limited to only active owners, but I mean I think the answer to your question is, there are a lot of large pass-through businesses that earn a lot of income. I mean these are the type of businesses that Brian represents.

I mean, you know, it's not just hedge fund managers, and other folks up there, there are -- you know, these are pass-through businesses with real employees, and real investment, and real profits. And, you know, there's a lot of income out there.

MS. FAULHABER: Right.

QUESTIONER: In fact there was a passive, someone had said --

MS. FAULHABER: The limitation is on the type of income, so if you're just getting interest and dividends, and similar types of income, the income can't be passive. But I agree that as long as you are a, sort of, hands-off investor in something that is getting active income, then you will end up benefiting from this.

MR. GALE: Yes, ma'am. The microphone is coming.

MS. GOODMAN: Colette Goodman from Goodwin. So, two questions: one, do you see the states moving toward changing their tax systems so that it will be more business-level tax, payroll, and so forth? And secondly, are corporations going to be low-hanging fruit for the states?

MR. REARDON: I'm not sure I understood the second part of the question. The first part I heard, I think every state that, you know, has income taxes is going to, over the next two years, adjust their taxes based on the bill. All the different provisions in there, and certainly the deduction is one of the big factors.

From our perspective, our goal is to increase the ability of S corps, partnerships, et cetera, to continue to deduct state and local income taxes. One of the

ways that that can happen, as I said, you know, under the bill if the entity pays the tax you get the deduction. So, one of the ways would be for states to allow an election for their pass-through businesses to pay the tax at the entity level, and therefore make it deductible.

So, we are working with folks to see if that's a viable alternative. So, you know, everybody is going to be adjusting based on the new laws, and I'm hopeful that some of those adjustments are friendly to pass-throughs. And the second part of it I did not --

MS. GOODMAN: Just given that the Federal made it so low now, and individuals can't deduct it, that the temptation is taking the increase (inaudible).

MR. REARDON: I think so. I don't know. And then, you know, I'll say, that's a political decision they are going to have to make, right.

MR. GALE: Mike, sure.

QUESTIONER: I mean the focus here -- Mike Scheyer -- the focus here has been on the difference on the difference between pass-throughs and corporations, and I think the real -- the rationality or the question is that, why somebody who is self-employed should pay a lower rate than an employee? Why should an employee of a taxi company pay a higher rate than the Uber driver? Or why should a doctor pay a higher rate than an engineer, for example?

I mean it's just -- I mean, it's the employees who are -- and in terms of state tax deductions, why should an owner of a pass-through get a state tax deduction when an individual employee doesn't? I mean, I think that's a more important comparison than the pass-throughs versus corporations.

MR. GALE: Do you want to respond?

MS. FAULHABER: Sure. I mean, I think that one way that you could, sort of, simplify down the distinctions between who benefits and who doesn't, is who has control, right? If you have the control that you can recharacterize yourself, either as an

independent contractor, or more likely as an owner of a company, and then you can have it -- you can be earning your income that would otherwise be wages through a pass-through.

There are some guardrails, but beyond that that gives you some control that there are -- that employees just don't have. And so that I think is a larger conversation about the role of employees in the United States, and the level of control that they are given, and the fact that they are not the ones who have access to a 29.6 percent rate, max rate, and that those who do have control are the ones who have access to that.

MR. GALE: John Sabelhaus?

MR. SABELHAUS: John Sabelhaus. So, this is for Lilian. Sort of picking up on a point you made in your opening remarks that this trend has been going on for a long time. I mean the wedge was put in place in 1986.

MS. FAULHABER: Mm-hmm.

MR. SABELHAUS: And yet we are seeing it, at just an exploding rate prior to the tax law, this shift over to pass-throughs. And I'm wondering, you know, as economists we think of that, okay, they do it to avoid double taxation, and other things. But it seems like there has to be something else that's going on. I wonder what your take on it is as a practitioner, and what that means for us going forward.

I mean, is it something about the ability to change what is taxable income, to offset positive, what we would think of as labor income with some sort of losses on assets? What is it that's really driving this shift, and what does that mean for us going forward.

MS. FAULHABER: Well, I will say that I'm an academic, so the practitioners the room might disagree that I'm not a practitioner anymore. But I think that there's -- you're right that there's a much broader story here, and it's not just about taxes, and I'll hand this over to Brian as well to see if he has thoughts about sort of what's

appealing outside the tax base to his members, but there's -- I think there are two stories that are going on, and there's the lower control story and the higher control story.

And the first story is the story about a lot of employees being shifted into independent contracting spaces, and that is tied to a lot of the other legal limitations that go with employee status and the sort of push away from that. And so I think you can see a lot of individuals cutting out of the protections of being employees who are now possibly going to fall into this space.

But on the fact that the majority of business income is now being earned through pass-throughs, in whatever form they are, so S corps, sole proprietorships, all of that, I think that in some ways there's been a greater awareness of both the fact that there are greater liability protections in some of these pass-throughs than previously existed, or were previously protected. And the fact that the double taxation has been, sort of, acknowledged and that there's -- you have a very large -- you have large entities that otherwise would have been corporations pre-1986, that have now been sort of accepted as being pass-throughs, and it's just become more common.

So, I hand it over to Brian to see if you have thoughts about sort of why that has happened.

MR. REARDON: Sure. There are certainly non-tax reasons why somebody might become an S corp, stay in S corp succession planning, ownership governance, things like that, but I think it largely is a tax story. And keep in mind that, you know, Congress, we created S corps in 1958, but we expanded the rules engaged in the early '80s, in '86 and '96, and 2003, 2004.

So, this has been an ongoing evolutionary process where Congress has intentionally spread the rules out so that more and more businesses could be treated as S corps. And, you know, there's this general perception out there that, you know, somehow they are getting away with something, they avoid the corporate tax. Well, I can just as easily say the corporations avoid the individual tax, right?

And these days that's pretty significant, right? You know, as C corp you pay 21 percent, S corp, or individually, you're paying 37 percent, right?

So, you know, each person, each business has to pick its entity and its structure based on what's best for it, but just because people choose to be an S corp doesn't mean that they're getting away with something or, in fact, that they're paying less than the C corp down the street.

In fact, my guys pay consistently in the 30 percent effective tax rate. And, you know, when you look at sort of the international rules in particular, a lot of these companies that they're competing with on the international front, are paying in the teens. So, my guys already pay a very high level of tax, under the bill that we just passed, you know, that disparity might even get worse. We'll just have to see.

MR. GALE: All right. One last question; my Co-Director, Eric Toder.

MR. REARDON: You had to pick him.

MR. TODER: If we assume that the reason we cut the corporate tax was largely for international competitive reasons, and the reason we didn't cut the individual rate was largely for revenue reasons, or we didn't cut it a lot. And so we have this big disparity. If we didn't have a special pass-through rate what would you suggest as a way of dealing with the disparity between the top corporate rate, and the top individual rate as alternative issue, policy?

MS. FAULHABER: So, so the question is: if we had not -- if we accept that there's a lower corporate rate had we not chosen a lower pass-through rate, what would be a better solution for responding to the disparity between the taxation of pass-throughs and the taxation of corporations; thoughts on that?

MR. GALE: Yes.

MR. ROSENBERG: I'm making sure Brian doesn't have anything to throw at me. But I mean, you know, the one answer is -- and again a point I think we agree on is, it might be nice to have a single way, a single tax system for businesses.

So, the answer to Eric's question might be that it's actually -- you know, it's currently very easy, or relatively easy for pass-throughs to elect to be taxed as C corporations.

So, if C corporations had such a good deal with the 21 percent corporate rate, you know, pass-throughs can take advantage of that. Now, there may be something they lose, non-tax through going to the C corp, you know, tax system but that's -- I guess that would be one answer. You know, the previous code and maintained in the Tax Cuts and Jobs Act is, in fact, a tax preference for pass-throughs relative to C corporations. Not all C corporations, not all pass-throughs, but I guess my simple answer would be, let pass-throughs be taxed as a corporation.

MR. REARDON: Well, a couple things. One, you know for years we've been advocating for the same top rate for everybody. Anytime you create disparities in rates you are going to have gaming and, you know, right now we have created a very large disparity, certainly through -- between individuals and C corps. But, you know, the different rates game is going to happen, and there are rules that they're trying to create and perfect to minimize that, but you're going to have tax planning around the different rates.

So, you know, our position has always been, a single top rate for everybody and make it a single layer of tax, eliminate the double layer of tax on C corps. In fact, we supported Senator Hatch's proposal to corporate integration, and I was a little disappointed that it never actually saw the light of day. In terms of, you know, can S corps just become C corps, yes, and many of them will under the new rules, but they are not in a better place, and the economy is not in a better place.

Let me just emphasize, and maybe that's, you know, something to close on, for me anyways, is you know all this tax plan that's going on right now within the pass-through world, and there's a huge amount of it, they are not making investment decisions, they are not making hiring decisions, the only hiring they are doing is KPMG, and PwC, and in firms like that, because they're trying to figure all this out, and until they

figure it out, they are not going to be making a whole lot of plans, right.

But if they do decide to go into the C corp world, they're not in a better place, because as a closely-held C corp, you're in a disadvantage compared to a publicly-held C corp. Publicly-held C corps have all the advantages, and so the idea that somehow, oh, they'll be okay. No, they are not going to be okay.

It won't be this year, it won't be 5 years from now, but 10, 15 years from now you will see more economic activity in the public sector, and less in the privately and closely-held business sectors. It's just going to happen.

So, those are the challenges that we face and, you know, I think that C corp rules and what they did is going to be a very significant positive for the American economy. I think what happened on the pass-through side, the best may be a push, maybe a little bit of a negative, we'll just have to see.

MS. FAULHABER: So, I think to bring those two together, I mean essentially Joe was saying tax S corps like C corps, and Brian was saying tax C corps like S corps; and I think that highlights the fact that I think the problem, the main problem here is just that it's creating these distortions based on entity structure, or characterization as an employee, or certain things where I don't think there should be distortions.

And so, I think ideally what you would want, if you would want to pull back, and you would want to say, we want to be able to have similar taxation regardless of your entity formation, regardless of your other legal status, and given that now a lot of pass-throughs have the same types, could have the same types, or do have the same types of legal protection as C corps, it may make sense to actually sort of pull back and reassess. Why we are taking, why we are putting so much emphasis the legal form and allowing such differential taxation when we could, instead, be focusing instead on who is really earning the money.

And that could take corporate integration, or that could take the form of

shifting, more in sort of shifting the two together, but I think that that's not what was done, and I think that the comments here have sort of suggested that from different perspectives, we all think that sort of focusing differential taxation on these formal definitions, or formal structures it caused a lot of the problems that were here. So, those would be my thoughts.

MR. GALE: All right. Great! I want to thank our panelists for elucidating an extremely complicated set of issues, well I should say, extremely complicated compared to most sets of issues, but perhaps not compared to the next issue we are talking about, (laughter) which is International Taxation.

So, let me just thank the panelists. And we'll get off the stage and we'll move on. (Applause) Thank you.

SESSION 2

MR. TODER: Okay. We are about to begin. So, if you were confused by the last panel, I can assure you that the material we are going to discuss now is very simple, and you will have no trouble understanding.

There is a handout in the packages which describes the new acronyms of international taxation that might be a little bit helpful, if you are following along. I also want to make a brief announcement. If you're following online, you can tweet under the hashtag BusinessTax.

And now my next job is to introduce the speakers. We have a really outstanding panel. Their bios are in your packet. I will just briefly say who they are: Pam Olson is, forget her title, Deputy Director of National Tax at Price Waterhouse, and she used to be Assistant Secretary for a Tax Policy at the Treasury Department, among many other things.

Rosanne Altshuler, is Professor at Rutgers University, and used to be Director of the Tax Policy Center, a very important position, and also was the Chief Economist on President Bush's 2005 Tax Reform Panel.

And finally we have Adam Looney, who is a Senior Fellow at the Brookings Institution, and recently was Deputy Assistant Secretary for Tax Analysis at Treasury, among many other things.

So, I'm going to start with Pam who is going to explain why we needed this reform; and Rosanne and Adam will try to explain what it did. And then we'll open it up to questions, for the panel discussion.

MS. OLSON: Okay. Thank you; and good morning, everyone. So, I think Chairman Hatch laid out a little bit of the rationale for tax reform, but I'll go into a little bit more detail. You know, first we had the highest statutory rate here in the U.S. relative to the rest of the developed world, the U.S. statutory rate came in at about 15 percentage points, above the OECD average.

We had a worldwide system with imposition of the tax deferred until profits were repatriated from offshore. That disadvantaged investment in the United States as a form -- now retired Tax Director used to refer to it, it was: the system was the 35 percent investment tax credit to keep my profits offshore.

The result was that we had about 2.5 trillion or a little bit more by a Joint Committee on Taxation estimate of foreign profits that were indefinitely reinvested outside the U.S. And then we had the impact of those two together on business decisions, and it really created an uncompetitive playing field for the United States when it came to decisions about where to locate the ownership of IP, where to locate operations, where to make investments and where to headquarter a business. And so, those were the reasons that I think we really needed, from a business perspective, to do a business tax reform.

Then I would say, putting on my Former Assistant Secretary of the Treasury hat, there were also some policy flaws with the system that, in addition to the business, what one would see as business flaws, and those were that the system provided limited protection of the U.S. tax base, an unlevel playing field for U.S. versus

foreign businesses.

And when you combined the highest rate in the developed world with the worldwide system, it resulted in global distortions as companies tried to avoid the impact that affected other countries tax systems as well.

And finally, I would say that we had really the lack of a stake in the ground on our jurisdiction to tax income. Another point to keep in mind is that this all occurred in the context of the OECD BEPS Project which was completed a couple of years ago, and which other governments were in the process of implementing.

The BEPS Project had four minimum standards on exchange of information, anti-treaty shopping, country-by-country reporting and dispute resolution. Those four minimum standards were things that the United States could implement administratively without a need to change the law.

But then there were a number of recommended practices that came out of the BEPS Project. Those included anti-hybrid rules, a stronger controlled foreign corporation rules, minimum tax, limitations on interest deductibility, aligning transfer pricing with value creation, and preventing the artificial avoidance of permanent establishments.

Those all required legislative changes in order for the United States to be able to implement any of those recommended practices to the extent that the United States chose to do so.

So, what came out of the Tax Cuts and Jobs Act? Well, a significant reduction in the corporate rate, obviously, from 35 to 21 percent, that brought the average -- our average statutory corporate rate, when you take into account state and local taxes, to the middle of the pack, to about 26 percent. That's approximately two points above the OECD average, so it was, I would say, a fairly responsible reduction in the corporate rate.

There's been a lot of talk about a race to the bottom when it comes to corporate rates, we clearly did not win that race, but you know we entered the pack that's

about a 1 percentage point below the OECD weighted average.

It converted us from a worldwide system to at least nominally, a 100 percent dividend exemption. I have colleagues who complain mightily that we shouldn't call this a territorial system, because there are so many provisions that apply now to international income that it's, in their view, not fair to call it a territorial system.

So, we adopted a 100 percent dividend exemption system that ended the disincentive to reinvest foreign earnings in the U.S. We also retained most of the CFC rules that were part of, you know, a prior law, and in some cases we strengthened them.

And then we imposed a one-time tax on unrepatriated foreign earnings as part of a transition to the new system, which removed -- and I think this is important -- particularly from the standpoint of confidence in the system as well as international -- of foreign governments' interest in taxing U.S.-based multinationals. It removed the financial statement target from those companies.

With respect to the policy perspectives, the implementation of BEPS, there were several base protection measures that were part of the Tax Cuts and Jobs Act, and in keeping with the season I would say that 2017 was Fat Tuesday, when it comes to tax planning, the Tax Cuts and Jobs Act significantly changes the landscape.

So, what did we get out of the Tax Cuts and Jobs Act on that side? Anti-hybrid rules, limitations on interest deductibility, a 30 percent of EBITDA transitioning to EBIT in a few years, with no relief based on a more favorable worldwide leverage ratio. So, we ended up with rules that are tighter than the rest of the world when it comes to interest deduction limitations.

Rules tightened on the transfer of intangible assets off shores. Again some strengthening of our controlled foreign corporation rules, and not one but two minimum taxes, and that's where you'll need your placeholder there with the acronyms. One, the global intangible low tax income, or GILTI for short; and then the Base Erosion and Anti Abuse Tax, or BEAT for short.

The GILTI and BEAT are both formulaic changes to how we tax foreign income, and together they'll significantly reduce both opportunities for and in the incentives of foreign tax-based erosion by U.S.-based companies, and importantly, protect the U.S. tax base from erosion.

Just a couple more words before I'm going to hand it over to Rosanne to give us some more details, but I think it's important to think about the policy rationale for the two minimum taxes. You know, if I were queen and could have written the rules I might have gone in the direction of saying, we need to fix our transfer pricing rules, we need to look harder at how we allocate the right to tax, and do a better job of staking out what should be within U.S. taxing jurisdiction, versus what should be in other countries' taxing jurisdictions.

If we go back to the House blueprint that was released almost two years ago now, June of 2016, that included a complete redo of jurisdiction to tax, because it focused purely on whether the goods or services were ultimately consumed in the United States. And if they were, then all the profits related to it would have been taxed here in the United States.

That idea never picked up steam, it became known as the "back tax", and the responders take on it: would you rather have a job or cheap underwear, never caught hold. And so, you know, we didn't end up with that redrawing of jurisdiction to tax, and instead we end up with a system that's kind of halfway there.

But so, you know, as the legislature was working, as Congress and the staff working on these, what became the Tax Cuts and Jobs Act, it was clear from both sides of the Congress that they were going to be significant changes on the international side. That neither side was comfortable with reliance on transfer pricing rules, or the ability to write better transfer pricing rules, and so instead we went in the direction of minimum taxes.

Now, minimum taxes are in some ways simpler, but there was a lot of

concern that a very strong minimum tax would put U.S. companies at a disadvantage relative to foreign companies that wouldn't be subject to the minimum tax.

And so what evolved was a less-strong minimum tax, that's a global minimum tax that hits the U.S.-headquartered companies. And then in addition to that, a second minimum tax the Base Erosion and Anti-Abuse Tax, or BEAT, that applies more broadly.

So, what the BEAT fairly -- it's going to have a lot of unintended consequences. All these provisions are going to have a lot of unintended consequences, but what it really does is to put both U.S. companies and inbound companies that are serving the U.S. market from outside the U.S. on the same playing field, and subjects their profits to a level of tax.

And so I think it was a really important step in the process, when both House and Senate came out with provisions that did, kind of, the same thing. And, so, with that I'll hand it back, and over to Rosanne.

MS. ALTSHULER: Okay. I guess I'll get into the weeds a little bit, and this stuff is kind of difficult, so I think I'm going to be a little bit repetitive. I can't stop myself from starting by saying something about the rate cut. It's a big deal, 35 to 21 percent. Pam has given you some context for that.

Not surprisingly, the standard deviation across countries on statutory rates has decreased, and that's important for income shifting and location incentives, that's also going to be the case for average tax rates. So, that's something to keep in mind.

Dividend exemption system, which was sometimes called, the territorial system, so we've moved to a dividend exemption system with anti-base erosion measures, which keep our system a hybrid between territorial and worldwide. And so we had a hybrid before, we have hybrid again.

But now, more specifically, we have dividend exemption or territorial for

low-margin foreign source income, and that -- low margin investments abroad, and a worldwide system, without deferral, current taxation for high margin foreign source income, with an 80 percent foreign tax credit limit with no carry backs and no carry forwards, and expense allocations.

So, let me -- I'll get back into that in a second. The deemed repatriation, as Pam, said as part of a transition to territorial, you have to think about what do you do with all of those earnings that are sitting abroad. So, we have a one-time toll tax on undistributed, non-previously-taxed foreign earnings. This is the big revenue raiser, on the international side. This is what makes it positive.

So, it's a 1.5 percent tax on cash and liquid assets, and an 8 percent tax on non-cash assets. It can be paid in installments over eight years, and foreign tax credits for the portion of earnings that are subject to the toll charge are going to be allowed. So, again, this is why the international package, together, raises revenue.

And then there is what Alan Auerbach, at a recent conference at Georgetown, called "presumed GILTI" minimum tax which I thought is great. So, GILTI is the -- I don't think Pam spelled it out. It's the global intangible low-tax income provision.

What's important is that it's not necessarily intangible income, we kind of back intangible income out, it's not necessarily low tax, but let's start outside of the weeds, and that'll explain that. So, it's a minimum tax on foreign source income, that's operated through a deduction, what I first have to do is define what GILTI income is. Its foreign income earned over 10 percent of tangible assets. So, it's a measure of excess returns over the 10 percent, which is pretty generous return on your assets abroad.

Marty Sullivan has written a lot of great stuff on this. He called that 10 percent, "pulled out of thin air". Now, I wasn't here when it happened, so I'm not sure where that came from, but once you've calculated that GILTI income you get to deduct 50 percent of it. Okay?

And it's going to be a 37.5 percent deduction after 2025. So, that

becomes a 10.5 percent minimum tax, but you only get credit for 80 percent of foreign taxes, and that the idea here is to retain the incentive to minimize foreign taxes that you pay abroad.

So, that brings the threshold for the minimum tax to 13.125 percent, that's the number that you need to remember, But it assumes, just as an aside, that the foreign countries are going to use the same base that we use, so that threshold isn't really a threshold. The idea here is to provide capital import neutrality for firms that are earning low or normal returns abroad, these are the firms that you would think are facing the most competition when they set up shop abroad, and then capital export neutrality for excess mobile returns.

So, that's the policy rationale. One of the things that is not so obvious when you first look at this, is that Congress kept the expense allocations rules that force multinationals to take some of the expenses on that they -- in the United States that are supporting the foreign operations, and allocate those to foreign source income.

And so that would be G&A, general administrative expenses, right, R&D interest. And so those expense allocations will still hold under the new law, and they go towards the GILTI basket of income, and it turns out the reason why you should be glad that you listened to me say all this, is because what happens, is you can end up owing tax on GILTI income even if you're in a country that has a higher -- even if your average foreign taxes is greater than 13.125 percent.

In fact, you can even pay GILTI if your taxes are greater than 21 percent. So, that's why it's not necessarily intangible income, because it's backed out, and it's not necessarily low tax income.

And it's an overall structure, so you take -- you don't go country-by-country when you're looking at whether or not you're above or below the 13.125 percent. You look over your entire operations; which means that if you are above that 13.125 percent you still have an incentive -- you know when you invest in a low-tax country, you

still get all the benefits of investing in that low tax country, and all of the incentives that existed before to income shift still exist in the low-tax country. So, it's complicated.

Then there's, FDII, so that's the foreign-derived intangible income. So, Congress took a carrot and a stick approach trying to attract intangible profits into the United States. The carrot is that this incentive under FDII, for domestic intangible investment. And the stick is a penalty on foreign intangible income.

And so what, really if you wanted just a short hand for FDII, it's a patent box, but it's not just on patents, it looks at the foreign share of returns above 10 percent on your tangible assets. So, it's kind of a perverse incentive -- if I have it right to -- you have the incentive to put tangible assets that are earning less than 10 percent abroad under GILTI, and you also have that incentive under FDII.

And again, it operates. It's a deduction, and so it gives you a 13.125 percent rate on foreign-derived intangible income, that's instead of the 21 percent rate.

So, the score would suggest that Congress doesn't think it's going to be used too extensively. It's not on foreign sales, per se, it's on you how much -- it's how much you earn on your foreign sales.

I think, one thing that I'll say about it, it's a -- there's still an incentive to put intangibles abroad it, depends on whether or not you're above or below that 13.125 percent, and it's certainly a windfall for those that are paying royalties back to the United States.

The problem is that it does not seem to be legal under WTO and there's going to -- it's an inviting a WTO challenge for sure, and if anybody is familiar with FSC DISC -- FSC/ETI, it looks like an export subsidy, and it looks like it's not going to survive. So I think there's a lot of uncertainty here.

And then I guess I'll just say a little bit about the BEAT before -- this is the global add-on minimum tax, it's aimed at foreign multinationals with operations in the United States. But as Pam said very well, it applies to U.S. and foreign multinationals.

You have to make a certain -- you have to be over 500 millions of gross receipts over a three-year period. You have to have a de minimis amount of related-party payments, but if you do you're going to pay an alternative minimum tax on your related-party payments. So, I think that's the easiest way to explain it.

Those related-party payments do not include cost of goods sold, so that does, of course, give you an incentive to vary fees for services and royalties paid to related parties into your cost of goods sold. The bulk of the burden is going to be on inbound investment, but it also does, of course, affect outbound investment.

So, there's a there's a problem here also, in that it may violate our treaties. So, it's not clear how long that's going to be around. Then there's the anti-hybrid -- really, just small problems -- anti-hybrid rules that Pam talked about, and then it's just to highlight again, we are going to be talking about what this does for incentives to invest abroad versus home.

At home, remember you're going to have expensing for five years, there's going to be this interest limitation that Pam talked about, 30 percent of EBITDA, going down to EBIT in 2022. And NOLs, net operating losses, we changed how those -- how you can use those under current law, that you can only offset 80 percent of taxable income, and there's no more carry backs.

So, a lot has changed, and I guess what we are going to get into soon, is how that affects income -- investments and income-shifting incentives. Okay, I'm turning it over to you.

MR. LOONEY: Thank you. So, I feel like we've covered a tremendous amount of ground already.

MS. ALTSHULER: Yeah, sorry, about that.

MR. LOONEY: So, I'll just say a few things. So, the first thing I want to say was, probably the most consequential choice in this reform, was the choice to retain the existing corporate system in broad-brush. So, what I mean is that we are going to

continue to tax corporations based on their residence, and the source of their profits.

That means that differences in tax rates across jurisdictions, and differences in the regime that is applied to corporations is going to continue to matter for where companies decide to locate, for where they decide to locate their operations. And further incentives about whether to try to avoid taxes, and how to do that.

And so in that world, that means that we are going to have to retain, essentially, all of the tax compliance, and administration apparatus that we had under the old regime. So, we still have all of our Subpart F regime, we have all of our foreign tax credit regime, and indeed we've added new minimum taxes onto that. And so the tax system is, it's at least as complicated as it was before, even if certain pressures are relieved.

And so again, in that world where taxes continue to matter for locational choices, you're in a world that is in some way, second-best. Where, we are going to continue to have to pursue these issues and police, in effect, the border. And where are the policy choices about what the minimum tax should be, or what the BEAT should be, are ultimately efforts to minimize or balance competing imperatives, and competing risks.

The second thing to say is that in the international tax world, the reduction in the corporate rate is a really big deal, because it takes a rate differential that used to be versus something very low, and reduces it to -- 35 on our side of the border, and something very low on the other side of the border, to something that's much closer to parity.

And so I think that in this discussion of international, we are going to focus on that as a good thing. Now, I think it's also helpful to remind ourselves that just, like, six weeks after signing into law a tax bill that is about a tax cut of about $250 billion a year, before it starts to phase out, we enacted spending increases of $150 billion a year before they expire.

And so, our long-term fiscal situation is, you know, it was bad to start

with, and it's much worse now, and so we are going to have -- we are going to need to have much more revenue, and we are going to have to get much more revenue from corporate income, either at the entity level, at the shareholder level, or when it is consumed.

And so I think, you know, I'm trying to differentiate the incentives about how the rate improves things on the international side. The dramatic rate cut in broader context is not an unmitigated good, and it leads to a lot of one's instability, I think, going forward.

But going back to that comparison of the level before and after; so clearly that there is a reduction in the difference in the tax rate that's paid on the U.S. side versus the foreign side, and yet there are still, clearly, issues that need to be resolved. And those are addressed in part by the minimum tax that was discussed previously, and the Base Erosion and Anti-avoidance Tax.

And so, just very briefly, on those things, the idea there is that if we are going to have a low -- a 21 percent rate on income on one side of the border for domestic U.S. corporations, we are going to have some provision that prevents them from easily shifting income or activities to a low-tax foreign jurisdiction to avoid the tax.

And so whether the new minimum tax achieves that, I think is a little bit unclear. It is the tax rate on the foreign side, is very low the base of that tax is very porous, and there seemed to be very -- a lot of opportunities to achieve a very low rate on foreign source income. And so I think that suggests that the incentives for profit shifting, for tax avoidance, and for locating certain types of activities abroad will persist.

Similarly, on the inbound side the problem, prior to this reform and continuing to some extent after this reform, is that a foreign-owned U.S. domestic company could achieve very low tax rates by making the deductible payments from the U.S. to a low-tax foreign company.

So, for instance, you could load up your domestic U.S. subsidiary with

lots of debt, pay interest to your -- to your Cayman related party and achieve a very low overall tax rate,

So, as Rosanne said, there are several provisions that attempt to reduce the opportunities for that 163(j) that provision that limits interest expenses, one that partly addresses that, the Base Erosion Anti Avoidance Tax also helps to reduce some of that. In that regard the tax rate might still be relatively low, and I think it's unclear whether some of those provisions will be able to go into an effect.

And so what I mean, I'm just going to give you one example. It's clear that under the Base Erosion Anti-avoidance Tax, some companies will pay the BEAT on their -- on income that is generating the United States, and then will be taxed a second time on that income whenever it accrues to the foreign parent. And I assure you the company, or the country where that company resides will want to pay that double tax. And so that's an issue that I think will need to be resolved, and I'm sure it will be litigated. And so I'll pause there.

MR. TODER: Okay. Well, let me -- First, I'll ask, does anybody want to add anything to anything anyone else has said?

MS. OLSON: I want to make one comment, and that's that one of the things that's really important to bear in mind here is that this is not a simple chess game with two parties, it's a multi-dimensional chess game and other countries are doing a lot to change their tax systems in reacting.

And so some of the things that have historically worked for tax planners have kind of been on the way out, because other countries have been implementing BEPS, and so it's going to be important to bear in mind what other countries do as we think about what the incentives are going to be on a going-forward basis; because some of the things that have been possible in the past are not likely to be continued to be possible in the future.

MR. TODER: Okay. So, there were two general complaints about the

international system kind of going, and one was it encouraged U.S. companies to invest overseas because of deferral and lower effective rate on overseas investment, and the other was that it put U.S. companies at a disadvantage because we do tax -- have this residual tax.

So, given that we've changed the way we do these things, are U.S. companies now at a smaller or bigger disadvantage than they were before? And is the incentive to invest in the United States smaller or bigger than it was before? And how much of those changes are due to the international rules, and how much just simply to the lowering of the corporate rate? That's a lot of questions at once, but -- and you can start Rosanne.

MS. ALTSHULER: I'll just randomly answer.

MR. TODER: Okay.

MS. ALTSHULER: I think that we've pushed -- so, first of all I think there's a lot of uncertainty, and I think instability here in the law that undercuts incentive effects. So, if you're not sure the provision is going to be around you may not, you know, repatriate your intangibles home, or something like that. That's just as an aside.

I think that overall, and I'll try to be quick, I do think that this pushes into the direction of making the U.S. more attractive, making firms -- making investment -- low return on investments, by low I mean under 10 percent, more competitive abroad. There's definitely an incentive to put your tangible assets abroad, there's more of an incentive to put your intangibles at home.

So, everything I think has gotten -- a way to summarize this, everything has gotten more compressed, but there are these kind of -- I don't want to say perverse -- but in terms of -- it really matters on the fact, on your facts, tangible versus intangible, what kind of services versus non-services. It's going to be difficult to figure that all out. But I think, the U.S. more attractive, U.S. firms more competitive, income-shifting less, things are compact.

MR. TODER: Okay. Do you want to --?

MR. LOONEY: Sure. As well, I think that there are two broad ways of thinking about this competitiveness. And so I think on one dimension, and the dimension that motivated this reform there's clearly an improvement.

So, I think that, as Pam said, that there was a perception that the U.S. was an unattractive place to locate a large multinational corporation. It was unattractive to do research, and to make large investments, especially investments that you plan to exploit by making sales globally.

And so I think that if you believe that having a very low effective rate on corporations encourages large corporations to locate in the U.S., and makes it attractive for them to grow here, then I think on that dimension certainly has worked. You know, it is a much lower tax country then it used to be, and much more attractive especially for companies that have a lot of overseas income.

I think on other margins, again there's not a perfect solution to this problem, and so I think on other margins there are clearly incentives, new incentives or enhanced incentives to locate certain activities abroad.

So, in certain cases that -- well, the tax rate domestically is still going to be 21 percent, in certain cases it will be possible to achieve very low tax rates abroad both because of the -- I don't know what the right term is, but they allow us for corporate equity that the 10 percent exclusion for income associated with tangible investment, and the ability to use excess foreign credits from a high-tax place to cover income from a low-tax place, there will still be very strong incentives for some entities to locate activities abroad.

And I think that those types of activities can be important. So, on that I'm not sure what the overall impact will be.

MS. OLSON: So, I think the 21 percent rate covers a multitude of things. I think that the willingness of businesses to restructure things, or to make investments

that they wouldn't make, absent taxes, has significantly gone down. And so I think that by itself does a lot to improve the competitiveness of the United States.

There was an article a month or so ago that kind of had a bad headline on it about the effect of the Tax Cuts and Jobs Act on investment in the United States, and the first two-thirds of the article were sort of all these bad things, and then the last third of the article was about all the good things that companies wouldn't be doing anymore, because of the reduction in the corporate rate that kind of puts the U.S. in the ball game relative to other countries.

So it makes it easier for you to source supplies and, you know, a long list of things that you're just not -- it's not worth the effort that you would have to go through in order to move some kinds of activities offshore with the significant reduction in the differential between the U.S. and other countries.

And again, I'm going to go back to what other countries are doing. There's a lot of effort outside the United States to grab a greater share of the profits of U.S. multinationals, and they are looking at it on a global basis. And this is like the U.S. Congress' response to some of that.

And I think it's one of the things that affects companies as they look at where they want to put their investment, because the United States is going to be a strong place for that investment to be on a going-forward basis, for profits to be generated on a going-forward basis relative to disputes that you might have with other countries over jurisdiction attacks.

And I also think that this is likely to be the first step in a longer discussion that we are going to have on the global stage about jurisdiction attacks. And if we look at the start of the BEPS Project there were a lot of loopholes, discontinuities, inconsistencies between tax systems that the project set about closing, but it didn't set about closing them with a view on, who got to tax the income.

That's a discussion that we still have to have, and in many respects the

Base Erosion and Anti-Abuse Tax, takes step in the direction of saying: let's look at destination bases as a way of deciding who has the jurisdiction to tax.

And so I'm going to take a more positive view on what's going to happen ultimately with this in the international space, about whether or not it's challenged by other governments, before the WTO, or that you know treaty violations are asserted, all of those things are definitely in the realm of what may happen.

But I think, you know, if you look at the continuation of the BEPS Project, there's a digital project that the OECD has picked up, and while it's supposedly focused on digital -- the reality is that the entire economy is digitalizing, and so it's going to have spillover effects. There the state aid cases, there are, you know, other governments that are enacting diverted profits taxes, and multinational anti-avoidance laws and, you know, taxes name for iconic American companies.

There's a lot of unhappiness around the globe with the way that the tax system functions, and I think this is the next step in the discussion and may well take us further into the conversation that I think we really need to have, about jurisdiction of the tax.

MS. ALTSHULER: So, that's interesting. So you see this as the provisions that clearly were going to invite problems with WTO, and GATT, as helping us go to a path towards destination-based -- a more destination-based taxation?

MS. OLSON: I think it definitely puts it on the table for a discussion. Yeah

MR. TODER: So, let me just ask one quick question. The 21 percent rate which -- us catching up with the rest of the world -- do you expect they will respond to that, and are we just joining a race to the bottom that will continue? And is this a first step in the erosion of the corporate tax worldwide? Or there are some countervailing trends that you see?

MR. LOONEY: I think it certainly is, and so I think that if I was in another

country and I was -- if I had spent the last 30 years and trying to reduce my rate below the U.S., after the U.S. reduced its rate in the '80s, I think that would seemed like that's what they did in the past. I think they have strong incentives to do it now.

I think around the globe, there are countries that are worried about how their patent boxes are going to work now that we have this new tax. And so I do think it provides that incentive. I don't think the mew tax we have really arrests that race to the bottom necessarily.

And also to say, is that this is a race that those other countries are much better equipped to engage in. They have much more robust personal income taxes, and shareholder taxes, or they have much more robust consumption taxes, and so they can weather a race to the bottom in ways that we can't, at least not with our current system.

MR. TODER: Okay I'm going to open this for questions. Joe? If you can just identify yourself, and ask a quick question, not --

QUESTIONER: The treaty as Rosanne mentioned, she thought there was a violation. I don't think there's any violation of the treaties. Was there anything in the law which indicated that the U.S. intended to override any conflicts with the treaties?

Adam seems to be the only person in the U.S. who is concerned about our revenue, and you did mention that there was -- was there any discussion of revenue sources? Like, Pam mentions that we are competing with these other countries all of whom, or most of whom have a value-added tax. And I've never heard one mention of a value -- or a value-added tax while this discussion was going on.

And the reaction of other countries, I've heard that China has already proposed tax reductions on profits earned on income which U.S. companies -- the cash which U.S. companies will leave in China instead of bringing it back to the U.S., and give them some tax benefits. Aren't other countries going to react viciously to our proposals?

MR. TODER: A lot there, that and other countries' reactions?

MS. OLSON: So, I think other countries have been reacting viciously for

a while, and this is finally the U.S. getting into the game with it, because I mean there's been so much going on around the globe, and we really haven't reacted to it because we haven't been able to legislate. You know, I do think -- I'm like Adam, maybe like you Joe, very concerned about the fact that we do, I think, need to raise more revenue in this country.

Maybe we can say that there's been an unmitigated discussion that we need to have about the size of government and what we want to you know raise taxes to cover, but clearly when you watch the votes being taken it would suggest that Republicans and Democrats are quite comfortable with the spending level that we've got, and therefore that means that we need to raise some more revenue.

And there is obviously one Senator who has been brave enough to introduce a value-added tax bill, Ben Cardin from Maryland, and testified before the Senate Finance Committee I think last summer, and lauded his bill and, you know, I think at that Committee hearing there were a number of senators from both sides of the aisle who said that they were willing to at least talk about whether or not there ought to be another revenue source.

I do think that we will fall short on the revenue side, I don't think we can get more money out of the corporate side, particularly if other countries respond by lowering their corporate rate, I think we've got to focus on tax, and what we can tax, and that's income that's less mobile than corporate.

MS. ALTSHULER: Yeah. I'm very much hoping that what this bill does is help us get to of a bat, because I think there are going to be problems with revenue, and I think that the question is: are we going to raise the corporate statutory rate? Or, we are we finally going to start really considering a value-added tax, which we will never call a value-added tax? So I believe like GST or something like that, or business activities tax.

MR. TODER: This lady has had her hand up for a while.

QUESTIONER: Yes. Good morning. Thank you very much. And I noted that, interestingly, Ms. Olson has actually been educated, at least academically, in the Midwest, so, which is unusual here at Brookings. But my question is --

MS. ALTSHULER: Get off the stage. (Laughter)

QUESTIONER: I'm sorry, but it actually -- my question has a Midwestern slant to it, because as Senator Hatch mentioned, companies that are offering one-time bonuses, but in fact in Wisconsin, Kimberly-Clark announced that it was using the tax plan as a basis for corporate restructuring, and was closing the two plants in what was historically its hometown, near Neenah, Wisconsin, resulting in a loss of 720 jobs in districts represented by Republicans.

So my question is, to what extent will other corporations like Kimberly-Clark use the tax code as a basis for eliminating jobs and moving them overseas, or just corporate restructuring?

MS. OLSON: So, my view is that the Tax Cuts and Jobs Act will indeed result in more jobs here in the U.S. than around the globe, because I think it shifts the balance that has favored foreign investment back to U.S. investment. But you know there's a lot of hard things going on in the economy, a lot of things that are unrelated to what happens in the tax world. And I'm not familiar with the situation you described, so I can't comment any further on that. But I do think it will be positive for jobs in the U.S.

MS. ALTSHULER: I think if we look really closely at a bunch of different firms, we'll see that the cost of investing abroad has actually gone up relative to 2017. So, I'm not so sure that this is going to be driving firms abroad.

MR. TODER: Yes? And after you we might have one more.

QUESTIONER: Raymond Aron Economic Policy Advisor. Just with, you know, as mentioned before that we used to have a hybrid in one sense, and now we have a new hybrid, and the incredible amount of complexities that are now associated with this new, you know, base erosion, anti-base erosion tax system, what would be the

problem with just coming at it from a more simple aspect of having a worldwide tax system with no deferral and calling it a day there?

MS. ALTSHULER: I'll let you go. I was going to say, we could lose all our companies, that's just one knee-jerk reaction, which is, it's going to -- so current taxation with no deferral at a 21 percent rate?

QUESTIONER: Yes.

MS. ALTSHULER: At the 21 percent rate. Well it's probably better than the current system, but I think it's not as competitive as we might like.

MR. LOONEY: I mean, if your question is motivated by simplicity, it's not clear that you really gain that much simplicity, you gain some, but I mean you still have to have a foreign tax credit system, and you still have to have a certain amount of rules. And then, I mean, I agree with Rosanne, you know, it makes it, if you're a business that's predicated on having a worldwide operation, and it does raise your effective rate for being a U.S. resident corporation, and so I'm sure that some companies, I don't know all of them -- but some probably --

MS. ALTSHULER: No. I mean, I wanted Rich Rubin to quote me.

(Laughter)

MR. TODER: Nice questions. Yes.

MR. CAMPBELL: Thank you. Leonard Campbell. If you could just speak to the incentive for not necessarily an established company, because I understand that it's difficult to shift everything around, but nascent companies to headquarter in the United States, given that the rate that we are talking about is pretty much middle-of-the-road, and the rules as we are in are fairly complex. I mean there are places where you could go where the rates are obviously lower, and the laws that you have to comply with are much simpler. So, what is the incentive to look at this as, you know, a great gift horse?

MR. TODER: I guess your question is, what is the incentive to

headquarter in the United States given that our rates are in the middle?

MR. LOONEY: I mean, so I think I actually don't know what the answer is, but I've got to say, one concern I do have is that in a regime like ours, with the minimum tax, and a minimum tax that applies a lot to intangible income, and if you have the next Facebook, do you want it to be a U.S. company. And it's not clear because, you know, you pay full freight in the U.S. and then you pay 10 percent around the globe.

If there was a way to get out of that system that might be -- if you could be somewhere else that might be more attractive. And again, I think that that's going to be determined in part by the worldwide changes that Pam discussed, that if those kinds of loopholes, or the gaps between real tax systems continue to close, then maybe there won't be at many opportunities for that in the future. But it does make me nervous.

MS. ALTSHULER: But we do have to think about how things were before this law, and I think that you have more of a reason to be here than you did before this law was put in place.

QUESTIONER: But what are those -- I'm not clear on it, and in fact I don't see --

MS. OLSON: The 21 percent rate?

MS. ALTSHULER: Twenty-one percent rate, and no repatriation tax.

MR. LOONEY: I mean, if your argument is like, if I can get zero somewhere else, then is 21 better than 35?

MS. ALTSHULER: Or, of course there's a slew of non-tax reason that we are not getting into, as to why you might want to be in the United States, headquartered. Yes.

MR. TODER: I'm afraid we are going to have to call it a day. So, thank you all very much. (Applause)

SESSION 3

MR. MAZUR: Okay. Let's get started with the next session for the

program. You have two guys in suits not used to wearing suits these days. So, it's a little bit uncomfortable for us being up here.

This is Richard Rubin, he's *The Wall Street Journal* Tax Reporter. I'm Mark Mazur, the Director of the Tax Policy Center. We'll have a quick little conversation, and then invite you all to participate.

So first off, Rich, you know, we actually grew up just a few miles apart in New Jersey.

MR. RUBIN: But you were educated in the Midwest?

MR. MAZUR: I was educated in the Midwest, yes, at Michigan State.

MR. RUBIN: I wasn't but, but its okay.

MR. MAZUR: But when you were growing up in New Jersey, at least when I was growing up in New Jersey, of course the people there that I grew up with, thought they would work in New Jersey, you get a job in a factory office around there, but you know you went pretty far afield. You ended up working at *The Wall Street Journal*.

MR. RUBIN: The Journal does have a large facility in South Brunswick.

MR. MAZUR: Okay. But you're not there.

MR. RUBIN: I am on there. Well, I was more of a faculty kid than a factory kid, so I think that this not like implausible, or out of the -- far out of the stretch, it's not necessarily -- I mean this became an option once centerfield wasn't an option, and then once second base wasn't an option. This was a good backup plan.

MR. MAZUR: And so how'd you wind up with taxes as the BEAT? That seems like a very specific area to work in?

MR. RUBIN: Yes. I started covering Texas in 2007. When I came to D.C., I was interviewing with the Congressional Quarterly and they had an opening covering defense and one covering taxes, and I was much more comfortable with numbers. And it's been, it's really, it's a fun thing to cover. I don't know why we get a full room of people interested in taxes.

You know, I like it because it's -- everybody has an opinion, everybody is affected by it, it intersects with everything, so I get to write about health care, about energy, about international relations, about things that are purely domestic in nature, I get to write about states, I get to -- you know, so it has -- and the other thing that's fun about it is it's, you know, you can write sort of big picture stories, and we saw this in the debate last year. Like we can write large about fairness, and equity, and all the sort of things that people like to think about, real broad strokes.

And then, you know, every layer you go deeper in taxes there's more stories deeper in the details as well, so you can get -- you know, the more comfortable you get in particular code sections there are really interesting stories about how businesses are changing, decisions, and based on how the law changes. So, it's both the depth, and the sort of big picture -- and the politics, I can be writing about politics too. So, it's got taxes --

MR. MAZUR: On everything.

MR. RUBIN: Touches on everything. You know, the motto is: taxes matter, but maybe not as much as you think, so right. So, going back to the question about, like where, you know, the nascent companies might want to have headquarters. It's like there are lots of none -- we all like to think, tax people like to think taxes, and there are lots of non-tax things that matter too.

MR. MAZUR: So, you've covered the Tax Cuts and Jobs Act from start to finish, the whole --

MR. RUBIN: Assuming it's over. Yeah. (Laughter)

MR. MAZUR: Two months or so. Did you expect there to be more tax reform in the bill as it went through? It turned out, really it seems like much heavier on the tax cuts part, than on the reform part.

MR. RUBIN: So, you'll know, if you read what we write, I'm studious about not using the word "reform" --

MR. MAZUR: I use overhaul.

MR. RUBIN: Yeah, I use overhaul, rewrite, revamp. Reform just has this, sort of, positive connotation, but we are among friends, so I'll I use it. And so I think, I think there's actually a lot of reform in there. I mean if you look at what the -- you may disagree with the content --

MR. MAZUR: A bit of reform.

MR. RUBIN: But what happened on the -- I mean, we all spent three hours talking about this, what happened on the pass-through side is a pretty significant reform of the way we tax businesses. What happened on the international side is a pretty significant reform. The limits on interest deductibility are a pretty significant reform, the limits on the state local deduction is a pretty significant reform. So, just probably 10 others, I mean, in fact you can't deduct entertainment expenses anymore, as a business, like you've barely written about that, right?

So, yeah, the balance tilted toward tax cuts and away from tax reform, but there's a -- if you only defined reform as revenue neutral '86 style, then no. But I tend to -- when I talk about it, I tend to think about it as, were there other structural changes and how, in what is taxed and who is paying. And yeah, there's a plenty of performers.

MR. MAZUR: Yes. I guess I would distinguish between structural change and reform, thinking reform being fairer, simpler, more efficient, and not so much on that side. There are a few. I think, you know, get rid of the charitable deduction for season ticket holders of major college football programs. So, it would be clearly, on the reform side, but the pass-through one it's arguable, right? That's just big structural change, but probably not simpler, probably not fairer, probably not more efficient.

MR. RUBIN: Yes. I think it depends, again, on how you define it, like it's fair, it's one of those words -- like reform is one of those words that it's in the eye of the beholder, it's a political choice, and so we can get sort of caught up in trying to figure out whether a new system is more or less fair, but it's actually -- and I can't -- I'm not going to

say the word "norm" --

MR. MAZUR: It's a normative kind of choice?

MR. RUBIN: Yes.

MR. MAZUR: So, when you were covering the Tax Cuts and Jobs Act, was there ever time you thought that it would not turn into law?

MR. RUBIN: Up until the middle of September is when my thinking flipped. So, I was, you know, in my head, all throughout covering this, and that goes literally since the day that I started covering taxes, I sort of keep in my head, like, how close are we to tax reform happening, and I don't think I -- I got over 50 percent in, like election night at 3:00 a.m., and then like reality set in.

And I'm like, okay. But I think, to me what really -- what flipped it was the deal that Senators Corker and Toomey struck in mid-September on the budget agreement. Like, until then it was not clear that, like they were still debating, like should there -- like, were they going to get a budget, was it going to be a real budget, was it going to have to balance, and that agreement, which I think surprised a lot of people when it came out, was really the -- said okay we've got this trillion-and-a-half, and that was, you could sort of see, it wasn't inevitable at that point, but it became more likely than not -- again a tax term, right?

MR. MAZUR: Mm-hmm.

MR. RUBIN: For people to sort of see how you could use that -- how they could use that one-and-a-half -- how they could use that 1.5 trillion to spread around and make enough great -- change that winners-to-losers ratio. Before that, if you were thinking about a purely revenue neutral, even revenue neutral on a dynamic basis, there still would have been -- the winners-to-losers ratio would have been really politically difficult, once they had 1.5 trillion to play with, you could see the path.

MR. MAZUR: It's always hard with the winners-to-losers ratio, right, because the losers are really sure that they're going to lose. That they think that they are

being disadvantaged whenever the law change, and the people who may benefit maybe are not so sure, and for sure are not going to raise their hand publicly and say, hey, I'm a winner look at me. And so the politics make it difficult to do, for when you sum this up as tax reform is hard?

MR. RUBIN: Yeah. But again, think about the winners-to-losers ratio and people not think, right. So, the TPC numbers in 2018 have 80 percent of households getting tax cuts, and 5 percent with tax increases. If you look at the polling, even polling today and certainly polling when they were voting, the people's perceptions of whether they would get tax cuts, not the perception of whether they thought the law was a good idea, which is a separate question, but perception of whether people got tax cuts were not quite the inverse of that, but pretty close to it.

So, that phenomenon was happening, but the fact that the actual winners and losers ratio, again, measured purely as tax cuts in the first year or not, it was so big that it meant that there were still enough people who thought they would get tax cuts to prevent the whole thing from collapsing politically, and Republicans sort of had the confidence to know that they thought that those -- that as people saw their withholding change, saw their tax bill change, got maybe not the bonuses, but eventually wage increases that the bill would become more -- if not popular, then popular enough to not be the anchor that it looked like it might have been in November/December.

MR. MAZUR: I mean that's one of the things that, a tax policy, and we tried to make the point that there was a different view on winners and losers depending on what time you looked at it. So, if you looked at 2018, we are pretty clear, like 80 percent of the people were getting tax cuts, and I think that's when Senator Hatch was giving us credit for helping them.

But then we said, you know, in 2027 when these provisions expire, it flips a different way, right. Lots of people have tax increases, and I think in the political world a lot of people heard that second part and didn't really believe the first part so much.

MR. RUBIN: Well, and I think that was the final version of the bill, it was not only one.

MR. MAZUR: Yes. Exactly!

MR. RUBIN: So, you know, the original House version, the revised House version, the first Senate version. So, I think there was probably -- I mean, I was bewildered during that six, seven weeks, I can't imagine people who were trying to follow this and figure out whether their own taxes would go up or down in any of the various iterations.

So, I think that was certainly part of what was likely causing some of the people's estimations to be of their own benefit, to be lower. And again, I don't know, when people answer those kinds of polling questions are they thinking: how am I going to benefit in 2018? Are they thinking -- you know are they influenced by their own political views of the bill even if they're asked specifically about their own tax bills?

And then of course the 80 percent figure includes the business taxes being distributed out to workers so, you know, some fraction of that 80 percent actually, if they look only at their own income tax will actually end up paying more, and not get a tax cut.

MR. MAZUR: So, what was the most surprising part of the Tax Cuts and Jobs Act?

MR. RUBIN: The speed, to me, with which it went from the first legislative tax to done, was really speedy. In 2011, in a previous job, I said to an editor, I said, we should really write a -- you know -- Dave Campbell was just taking over, and he was talking about various -- you know, his plans. And I said, we should write a story about the importance of transition rules, and there's going to be this big lobbying effort around trying to make sure that transition rules are set up to, you know, businesses are really going to lobby to push for specific things that are helpful to them to smooth out the first couple years in a new system.

The editors were, no, no, no, no, it's too soon, it's too soon to do that. So, I never wrote the story, and so I never actually -- I meant to write it at some point in November/December, as I said, transition rules are important, businesses have lobbied for them, and some of them got them, and it's just -- but the speed of the process meant that we just didn't get to write stories like that.

And so even things like the international system, someone said it earlier that like -- no, the Chairman said it, right, that there hasn't been, you know, enough attention paid to the international, but part of that is because they went from the period of time between when the Senate version, which actually had the BEAT and the GILTI that was ultimately the bill, came out November 9th, and it was signed into law on the 22nd.

MR. MAZUR: Without like a serious hearing to go through each of those provisions?

MR. RUBIN: Right. I mean the problems we'll argue, correctly, that they've been talking about territorial systems for a long time, right. And that's true there was plenty of discussion about the concept, and people talking about minimum taxes, but the actual structure of what they did, is actually being debated more now, than it was in that six or seven-week period when they were writing the legislation. And that's just, there was just too much else to do.

I mean, you know, we did what we could, but there's, you know, five, six different versions, important things affecting individuals, the pass-throughs, the states, there was all the politics that was going on, there was just -- and so what surprised me was the sort of intense flurry of how fast it happened and how -- not that it prevented people from looking at it and thinking about it, but the more detailed and technical the provision was the less attention it necessarily got and that in that compressed window.

MR. MAZUR: So, in the age of social media, you've been a consistent contributor to Twitter, you're a contributor to the live blog at *The Wall Street Journal*, what is different dealing with social media compared to traditional journalism? Or, how has

traditional journalism changed in the era of social media?

MR. RUBIN: I mean it's great! You know, liked it -- so, it was really an intense six to seven weeks, but I, like all the time, I'm getting, it's you get this instant feedback loop of ideas, and thoughts, and comments, and so I write something, and I'd hear back -- you know, in email or phone calls, Twitter, whatever. I mean, I had to get used to, during this process to texting sources, which I had never done really before, but I did.

And so you get -- it actually made the whole thing, despite the fact there was a lot of stuff that we weren't able to get to in that compressed timeframe, the ability to move faster, and publish faster, and think faster. I mean it helped, I get ideas from everywhere, from experts and non-experts alike.

MR. MAZUR: And you're even branching out to video too?

MR. RUBIN: Yeah. We've been doing tax explainer videos which people actually watch, and again because people care, and so it so, you know, what we are trying to do is reach both a sort of tax audience, and do things that are accurate and helpful for a tax audience, but also that reach out to our broader audience that is interested but not necessarily technical tax people.

This feels very strange for me sitting here and answering questions instead of asking you questions, by the way. (Laughter)

MR. MAZUR: So, do you do your own taxes?

MR. RUBIN: I don't.

MR. MAZUR: You don't?

MR. RUBIN: No. Do you do your own taxes?

MR. MAZUR: I do. I do TurboTax but -- because Commissioner Rossotti, when I worked there reminded me that my time was more valuable, and instead of being a scribe and writing numbers down, I should use the software and file electronically.

MR. RUBIN: No. I don't. I figured that -- and probably IRS people are probably watching this -- that I don't want to do anything to invite extra scrutiny, so having an extra set of eyes on my return is probably a good idea.

MR. MAZUR: And so what do you do in your free time away from taxes?

MR. RUBIN: Taxes. (Laughter)

MR. MAZUR: No, someone else does your taxes; now, really, serious.

MR. RUBIN: I read, I like baseball; I try and get away from taxes ever so often.

MR. MAZUR: Yankees fan? Mets fan?

MR. RUBIN: Nationals fan.

MR. MAZUR: Nationals fans?

MR. RUBIN: Yeah, yeah, yeah.

MR. MAZUR: I can see some cheering over there. The last question I have, and then we'll turn it out to the audience. Are there any journalists that you, like, especially admire?

MR. RUBIN: Let me just offer a word of praise for everyone who was covering the tax bill last year, it was an exhausting, and long, and tough process for all of us, and there's a lot of really great -- and I don't want to name people, because I feel like I'd be leaving people out, but there's a lot of really good coverage.

I can't tell you the number of times in that, I mean all of last year, but especially in that six to seven-week period when the bill was live, when I read something, and I was like, ugh, I meant to write that, or I should have thought of that. So, all the time there's lots of really great and smart coverage out there.

You know, I didn't read or watch everything but there was -- you know if you were following the bill you were able to get a lot of information -- if you were following closely, then you knew where to look, really, you were able to get a lot of really good information.

MR. MAZUR: Mm-hmm. Okay, maybe we'll open up to the crowd for questions. You sir, way in the back, the microphone is coming.

QUESTIONER: Richard, did you have a sense of who was making the decisions, the big decisions, and small decisions during this fast and opaque process? The usual suspects are Tax Writing Committee or Chairs, political leaders of the House and Senate, the White House and Treasury. Last weekend the leading technician from Treasury discounted his input saying, Treasury had very little input, they sat through drafting, but very little input. How were decisions being made?

MR. RUBIN: Quickly, I think there were -- so in the House you had Chairman Brady and his Committee staffs were really owning their part of it, with input from leadership staff. And on the Senate side you had the Chairman and his staff, and the leadership policy staff, as well as, you know, they appointed four or five senior Finance Committee Members to work orchestrate the thing.

And it's Thune, Toomey, Portman, Scott and Cornyn, who sort of were able to cut a lot of those deals, you know that -- And so, largely that's who was making the decisions. I mean, Treasury was involved, but I didn't sense a lot of Treasury in like technical input at the time, Joint Tax was involved, but they're not, you know, they advise and don't necessarily make the decisions.

But this was part of possible heart of the 51 votes, and so -- and it was, you know, its members, there were many things that were member-level decisions, but it's a pretty small group of senior staff that guided the process.

MR. MAZUR: Emily .

QUESTIONER: Thank you. You mentioned a couple of things that you counted as reform that hadn't gotten a lot of attention. One thing that I've been made aware of, and I may not know -- have all the details right but it has to do with the tax deductibility of salaries in excess of $1 million, whether that's deferred income, whether that's stock options coming into fruition, or whatever.

How do you see that? I've seen nothing written about it. I know at least in one instance the impact of it could have a pretty significant effect on what the tax rate is for the company itself, and they're not a very high-paying company, so I was sort of amazed at that. It could have larger impact on competition, how people think about comp, you know what you do in as a Board Member on a Comp Committee thinking about, you know, how competitive you're being, and so on. What kind of salaries you want to pay, how you want to pay them. It seems to me this is something that should be interesting to people, but it hasn't been covered.

MR. RUBIN: We've written on it some, and I'm sure we are going to be writing on it some more. We had a story just last week, I think, on the nonprofit side of this, about there's a similar cap that got imposed on a nonprofit compensation over $1 million, and so we had a piece that looked at a non-profit hospital compensation and the way it sort of works, definitely depending on how unified your entity is. If you are split into a bunch of nonprofits, then each of them might be subject to the cap on its five, the top five employees, as opposed to if you were a unified system.

So, I'm sure we'll do more of that, broadly what it did is, as you presume, you know, is that there used to be a sort of an exception for a performance-base -- deductible performance-based pay over a million, and now that's limited that, I'm sure that's one those areas that tax lawyers were trying to find --

QUESTIONER: The answers --

MR. LOONEY: Yeah. And so, I'm sure that's something we are going to be looking at more.

MR. MAZUR: The person in the middle here, in the blue shirt. The microphone is coming, here you go.

QUESTIONER: So, if we are looking at policy-making as a tennis match, and not a collaborative, and you talked to some Democrats during this process, say, they come back into power. If they want to get more revenue for priorities they, traditionally,

favor. To what degree could they walk back the corporate tax change? And to what degree wouldn't be able to because of the international situation, and then where else could they look?

MR. RUBIN: I think that is exactly the questions that -- that's a great question because it will shape how Democrats view this, in part, in going into this year's campaign, but what I'll watch for is the presidential candidates for 2020, because it's the most likely time when they'd actually be able to do something, would be if they had unified control of the government in 2021.

And I think you'll see a split. As the Chairman said, although he kind of went a little farther than the reality of it; there are Democrats, there are a lot of Democrats who wanted to cut the corporate tax rate, and so what may not be the case, that that's the lever that they would want to pull, certainly -- or even if that's were some of them want to go, there might not be 51 democratic votes for 25 percent, 28 percent, whatever.

So, I pay attention to what the levers might be. You can look at changes on the international structure, you know, dialing those rates they could look at cap gains and dividends on the individual side, the rate structure on the individual side. There's a lot of different ways they can go with this, and I'm going to be watching, and writing, and curious about exactly where different factions within the Party go.

You know that there hasn't been a lot of: we must repeal it right away, kind of arguments. I think you'll see a much more, (a) keep the things they like, and try and pare back the things they don't.

MR. MAZUR: You have a natural time, right, at 2025 when the individual things expire, you can come back and revisit it at that point, perhaps writ large.

MR. RUBIN: Yes, but I think one thing that we've seen the way that policymaking happens is that members know that if they're in that situation when they have control of the House, the Senate and the White House, they're going to go with the -- you know, I cannot tell you how many times I heard the: failure is not an option, perfect

can't be the enemy of the good. Like that was the motto of Republicans in the fall of last year and so, you know, they know how short the policy for all the big you know -- the planning people at Brookings who have, like written books and papers on why the modern Congress is this way, but that's -- like it's ingrained in their minds that if they have control they are going to pick the top two or three priorities, and do as much they can.

MR. MAZUR: Okay. Eugene Steuerle, back there?

MR. STEUERLE: Hi. Eugene Steuerle, at Tax Policy Center. I was thinking to raise it at the other sessions, but it didn’t quite fit, so it's probably not a fair question to ask you. But is there any thought given to the situation of new businesses, start-up businesses, relative to established businesses in this tax bill?

I know we worked on the tax reform in the '80s one of the things we pushed and actually trying to -- for instance establish depreciation allowances, was that expensing, really disfavored the new business that could ever use the deductions, and I've even thought out how this plays out on the international front. So, I'm just curious whether that's a topic that you or someone else might be reporting on?

MR. RUBIN: That's a good set of questions. I guess, the full expensing would seem to benefit new capital versus opposed to old capital, but as you point out, if you are spending a lot of money upfront, you may not be able to get to use all of that right away, and NOL limits will play into that somewhat too.

I don't know. That's a good set of questions about where the incentives are for new business, and whether you would want to set up in pass-through form or corporate form too.

MR. MAZUR: Okay. Up here in the middle.

MR. CHANDLER: Thank you. Gerald Chandler. Off the record, what have people in Congress told you about entitlement reform? (Laughter) And on the record, do you think anything can be done before the country runs out of money?

MR. RUBIN: So, I'm not going to share any off-the-record conversations

I've had, but I also don't really -- you know, it's one of the limitations that we have as I cover taxes, in probably like blinder a bit, so I don't know. I think this is one of those -- I would argue that the bill that passed last week probably makes entitlement reform, and there's that word again, less likely because, you know, you've got Democrats who will say: wait a minute, we just spent a whole bunch of money on that, well, like why can't we do that over here too?

To me, it seems any sort of major entitlement bill seems farther off than it was. I don't know what the triggering event is for some sort of change of mind on that.

MR. MAZUR: Well, thank you very much, Richard. Appreciate you coming here. Please join me. (Applause)

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