Bond Case Briefs

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State Deduction Among Possible Targets If ACA Taxes Axed.

Republicans could try to eliminate the municipal bond interest tax exemption or the state income tax deduction after the failure of the House GOP health care bill undermined their ideal tax reform baseline.

Repealing the Affordable Care Act and its taxes had been Republicans' plan to find the savings for a revenue-neutral overhaul of the tax code, ending billions of dollars in spending on credits and subsidies and lowering the baseline to make tax reform a little easier. Since that effort fell apart, lawmakers may have to turn to alternatives.

"The question hinges on whether lawmakers will now seek to repeal some or all of the ACA taxes," Scott Greenberg, an analyst at the conservative-leaning Tax Foundation in Washington, told Bloomberg BNA.

The taxes include net investment income and medical device taxes.

U.S. House Speaker Paul Ryan (R-Wis.) withdrew the GOP-authored American Health Care Act March 24 when it became clear it lacked the votes to succeed. Ryan and President Donald Trump said they would move on to tax reform, returning to health care later.

"If lawmakers do try to repeal the ACA taxes as part of tax reform, then the budget math will become more difficult, and they may need to look more seriously at unpopular measures to raise additional revenue," Greenberg said.

Alternatively, lawmakers could decide that ACA taxes shouldn't be repealed until the health law itself is. In that case, the budget math for tax reform shouldn't be any harder as a result of the failure of ACA repeal, he added.

Hard to Predict

Charles Henck, an attorney and partner in the Washington office of Ballard Spahr LLP who specializes in tax matters, told Bloomberg BNA that the exemption for municipal bond interest and the state and local tax deduction are probably safe, but that he wouldn't be surprised if they were on the table.

"Predicting what Congress will do" is nearly impossible, he said, adding that municipal bonds, a popular method used by states and local governments to pay for roads, bridges and other public projects, often come up in congressional tax reform talks.

Border Adjustment

Other factors are at play for states. If Congress doesn't pass a border-adjustment tax, that also could put exemptions and deductions that states care about in jeopardy.

"If the border-adjustability piece, which raises close to a trillion dollars, is not completed, and we've heard mixed views on that, then everything is on the table," including the exemption for municipal-bond interest, said Jim Febeo, senior vice president of government relations at Fidelity Investments.

In general, imports would be taxed and exports would be exempt under the border adjustment plan.

Revenue-Neutral Goal

All of these issues are interrelated, even more than they otherwise would be, because Speaker Ryan and Senate Majority Leader Mitch McConnell (R-Ky.) have said they want a revenue-neutral tax plan so that it can pass the Senate with just 50 votes. Vice President Mike Pence could provide the tie-breaking vote, if needed. The picture is in flux, however, and some lawmakers have said they are less committed to revenue neutrality in a tax bill.

Scott Pattison, CEO of the National Governors Association, said his organization is asking congressional leadership to consult with governors on issues that might impact state budgets. The group and individual governors have been very active this term reaching out to House and Senate members, as well as the White House, Pattison said.

He said he has been pleased with the reception governors have received from lawmakers.

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