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OUTLOOK: Tax Reform Bill Unlikely But Muni Market Must Remain Vigilant.

WASHINGTON – Congress will not act on comprehensive tax reform next year, but House Republicans could try to move forward with international or corporate tax reform, according to tax experts.

In any case, muni market groups must remain vigilant in educating lawmakers about the importance of municipal bonds, the experts and market participants said in interviews about 2016.

“There will be no important tax legislation next year, nothing’s going to get to the finish line,” said Howard Gleckman, senior fellow at the Tax Policy Center.

Senate Majority Leader Mitch McConnell, R-Ky. “has made it clear that it’s a nonstarter and Obama’s just not interested,” he said.

Just after he replaced John Boehner as House Speaker, Rep. Paul Ryan, R-Wis., said he wanted the House to pass a tax reform bill by July 18-21, when the Republican presidential convention is to be held in Cleveland. More recently Ryan said it would impossible to do comprehensive tax reform while president Obama is still in office, but he did not close the door on international or corporate tax reform.

“I understand Ryan’s enthusiasm,” said Gleckman of the former House Ways and Means Committee chairman who was, and is expected to continue to be, very focused on tax reform. “I just don’t see it.”

Several congressional observers said that by enacting the $1.1 trillion omnibus spending bill and the tax bill this month, lawmakers do not have much left to do next year.

“Everyone would agree that what Congress ended getting done at the end of the session was a larger package than expected,” said Micah Green, a partner and co-head of government affairs and public policy group at Steptoe & Johnson. The tax bill extends expired tax provisions through the end of 2016, he said.

“Congress has basically completed its to-do list,” said John Godfrey, senior director of government relations at the American Public Power Association. “The pressure to act has been lifted.”

However, Godfrey cautioned that tax policy is driven by headlines as well as deadlines, and said that if there is more controversy over U.S. companies moving their headquarters overseas to avoid U.S. taxes, that could spur efforts at international tax reform.

New House Ways and Means Committee Chair Kevin Brady, R-Texas, recently told reporters he wants to focus on international tax reform in 2016 and set the stage for a broader tax overhaul after the presidential election. In November, just after replacing Ryan, Brady said he planned to solicit the views of House members on tax reform over the next few months.

“I suppose you could see a scenario where there is agreement on international tax reform,” said Green. “But as you build up to the elections, making hard choices is harder and harder to do.”

“I don’t think we’re going to see anything in the form of comprehensive tax reform until after the elections,” said Jessica Giroux, general counsel and managing director of federal regulatory policy for Bond Dealers of America. “I think there will continue to be discussions.”

“There are two areas of risk,” said Michael Decker, managing director and co-head of municipal securities at the Securities Industry and Financial Markets Association.

First, in broader discussions on comprehensive tax reform, tax-exempt interest “will most certainly be on the table,” he said.

Second, if some form of tax reform legislation that is not comprehensive is considered and there is a need for revenue raisers to pay for provisions, “there’s always the risk that some tweaking of the tax-exempt bond statutes will find itself in that discussion,” Decker said.

“Even if you don’t have comprehensive tax reform there’s still substantial risk that municipal bonds will be on the table for corporate tax reform as a pay for,” Godfrey agreed.

Bill Daly, director of governmental affairs for the National Association of Bond Lawyers pointed out that corporate tax reform could very well involve munis, as there are tax provisions that limit the amount of tax-exempt bonds that some companies like banks or insurers can hold.

But he added that, “It’s hard to see [Congress] doing much with the truncated session” for next year’s presidential election. Members will be out part of July, all of August, all of October and most of November.

Still, he said, “The muni market needs to be vigilant no matter what.”

Green agreed. “I’ve always said that the time to make the case for the value, the efficiency of municipal bonds is before there’s movement on tax reform,” he said.

Muni market participants in past years have had confront Obama’s repeated budget proposals for capping the value of tax exemption at 28% for higher income earners. Former House Ways and Means Committee chair Dave Camp in 2014 released a draft comprehensive tax reform proposal that would have imposed a 10% surtax on muni bond interest for higher earners and eliminated the tax exemption for new private-activity bonds.

“Once you’re on the menu, you’re always on the menu,” said Godfrey.

Giroux said BDA is going to continue to try to educate congressional staff and members about the importance of municipal bonds. She said she assumes the group will do another educational seminar for staff next year.

Obama and other lawmakers have proposed reinstating direct-pay bonds like Build America Bonds, but with lower subsidy rates.

“We think you can make a strong argument to revive BABs,” said Decker. “But there seem to be key members of Congress that just don’t like that product and if that continues to be the case, it’s hard to imagine there’d be much movement in Congress.”

Both he and Giroux said BABs have lost some support among issuers because of sequestration, which has reduced their federal subsidy payments. “Sequestration needs to be addressed,” said Decker.

Asked about some lawmakers’ attempts to push for more tax credit bonds, Decker said, “It’s just a structure that doesn’t work well, that’s never been proven even on a small scale basis.”

When Congress in 2010 offered certain bonds in both direct-pay and tax credit modes, and allowed issuers to choose between them, none chose tax credit bonds.

Gleckman said rising interest rates may take more of the spotlight than tax reform in 2016.

“Probably the most important thing in the municipal market is the Federal Reserve Board and what’s going to happen to interest rates.”

If the Fed continues to raise rates, he said, “It’s going to make it more expensive to borrow money” and it’s going to “close the window” on advance refundings.

THE BOND BUYER

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