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Tax-Exempt Bond Market Left Worried by Proposed Trump Tax Plan.

WASHINGTON – Trump administration officials outlined a sweeping tax reform plan involving cuts in tax rates that would be paid for by economic growth and the elimination of tax deductions and loopholes for the wealthy, leaving municipal market participants in fear of losing the the tax exemption for municipal securities.

Top White House advisor Gary Cohn told reporters that the administration is proposing to save the deductions for mortgage interest and charitable contributions as well as the exclusion for retirement savings. “Other tax benefits will be eliminated,” he said, telling one reporter later that includes the deduction for state and local taxes.

Neither Cohn nor Treasury Secretary Steve Mnuchin specifically mentioned the tax exemption for municipal bonds. But market participants raised concerns about the exemption, which is a tax exclusion.

The one-page briefing paper handed out by the administration said, “Eliminate targeted tax breaks that mainly benefit the wealthiest taxpayers.”

Critics of tax-exempt munis have said they mostly benefit the wealthy, although municipal market participants contend they are critical for financing infrastructure.

“If accurate, we now know the Administration’s opening bid on muni bond tax exemption (unless preserved under infrastructure plan),” Ernie Lanza an attorney with Clark Hill tweeted.

“I think this should give pause to the industry because the tax exemption for municpal securities was not specifically mentioned in today’s announcement,” said Curt Beaulieu, senior counsel at the Bracewell law firm and former tax counsel for the Senate Finance Committee. “Based upon what we heard, one can deduce that the tax exemption for munis would be eliminated.”

“We should assume we are in play,” Chuck Samuels, with Mintz Levin, said referring to the muni tax exemption, “It makes no sense for the tax plan to marry tax reform with infrastructure and then restrict municipal bonds, but we should assume the worst.”

“The tax-exempt bond community is as organized as it’s ever been. We have lots of resources and ammunition and we’ll need to use it,” he added.

One concern for the muni market should be that tax experts say the Trump plan would be so expensive and administration officials are so unrealistic in thinking it could be partly paid for with strong economic growth, that there will be a huge need for revenue raisers to be used as “pay fors.” Historically lawmakers have looked at restricting tax-exempt muni bonds to create revenues. The Tax Reform Act of 1986 included a host of muni bond restrictions.

Tax experts also say the administration would have such a difficult time making this plan revenue

neutral, that if it wants to push forward under a reconciliation bill that would need less votes in the Senate, the provisions would have to be temporary and last no more than 10 years.

This is the most significant tax reform legislation and one of the biggest tax cuts since 1986, said Cohn.

The plan, which Mnuchin and Cohn stressed must still be negotiated with the House and Senate, would reduce the seven personal income tax rates to three — 10%, 25% and 35%, while doubling he standard deduction for married couples. The top tax rate for individuals is now 39%.

“We are creating a zero tax rate for the first $24,000 of a married couples’ earnings,” said Mnuchin.

The plan would repeal the alternative minimum tax, which applies to most private activity bonds.

It would phase-out of the death tax and eliminate the 3.8% tax on capital gains and dividends that President Obama added under the Affordable Care Act.

The administration will reduce the rate on corporations and pass-throughs to 15% from 35% and wants a one-time tax on the repatriation of overseas earnings, but Mnuchin made it clear there will be an effort to focus on small businesses and prevent big firms from setting up pass-throughs to get the 15% rate.

Cohn and Mnuchin said they plan to hold “listening sessions” on the plan and will work with the House and Senate on legislation.

House and Senate Republican leaders said in a release that the principles released by the Trump administration are “critical guideposts for Congress and the administration as we work together to overhaul the American tax system and ensure middle-class families and job creators are better positioned for the 21st century economy.”

But Rep. Richard Neal, the top Democrat on the House Ways and Means Committee, said in a release, “President Trump’s tax proposal does not do nearly enough for working families and small businesses in this country. The tax cuts proposed by President Trump would disproportionately favor the wealthy and large corporations at the expense of our nation’s hardworking middle class.”

Rep Lloyd Doggett, D-Texas, ranking minority member of the committee’s tax policy subcommittee, added, “The claim that his multi-trillion dollar tax cut will pay for itself is as incredible as the claim that Mexico will pay for his multi-billion dollar border wall. Dripping in red ink, this proposal validates Trump’s boast that he is ‘the king of debt.”

The Bond Buyer

By Lynn Hume

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