THE BOND BUYER
Thursday, July 28, 2016 | as of 2:43 PM ET

Taxation

Groups Urge GOP to Maintain Muni Exemption in Tax Plan

By Evan Fallor
July 27, 2016

WASHINGTON — Municipal issuer, education and utility groups are urging Republican lawmakers to maintain the tax-exemption of municipal bonds in their blueprint for tax reform.

The groups submitted their concerns to House Ways and Means Committee chairman Rep. Kevin Brady, R-Tex., and House Speaker Rep. Paul Ryan, R-Wis., who released the GOP blueprint for tax reform on June 24 under Ryan's "A Better Way" agenda.

The blueprint makes no direct mention of munis, but suggests repealing unnamed exclusions, deductions and credits. Ryan has said the plan will continue to be amended before Republicans introduce formal tax legislation next year.

Municipal Bonds for America, a coalition of issuers and government officials, said in a July 15 letter to Brady and Ryan that munis have been the "primary financing mechanism" for public infrastructure projects for more than a century. The organization said it opposes any legislation that would tax munis, claiming this would increase costs for roads, water, school and airport improvements as well as other public projects.

"Attempts to curb or repeal the municipal exemption would dramatically increase the cost of infrastructure projects to the detriment of the public who will have to bear those increases, and undermine the efforts of America's state and local governments to move their communities forward," the group wrote.

Similarly, Bond Dealers of America sent a letter to Ryan and Brady earlier this month stressing that an elimination of the muni exemption would cost state and local governments an additional $495 billion in interest over a ten-year period.

The Education Finance Council (EFC), a group representing nonprofit and state agency student loan organizations, also wrote to support the tax exemption. EFC president Debra Chromy sent a letter to Brady and Ryan on July 20 urging the lawmakers to maintain the muni tax exemption because of the lower borrowing costs it provides students.

"Tax-exempt bond financing typically results in reduced loan costs to the borrower because interest on the bonds is not subject to federal income taxes," Chromy wrote. "Repealing the municipal exemption would dramatically increase the cost of these education loans, adversely affecting our nation's students and families, who already bear the burden of $1.3 trillion in student loan debt."

EFC lauded the blueprint's proposed elimination of the alternative minimum tax, which it said would lower costs for education loan borrowers. It cited Congress' temporary elimination of the AMT on income earned from private activity bonds in 2013, which it said resulted in lower borrowing rates for student loan issuers and cost savings for student loan borrowers.

The broad nature of the blueprint released by the Ways and Means Committee's Task Force on Tax Reform has sparked concern among muni market officials who feel mean reforms for the muni exemption, which has been in place since 1913.

The blueprint would reduce the corporate income tax rate to 20% and reduce the current seven-bracket individual income tax rate to three brackets of 12%, 25% and 33%. On top of eliminating the AMT for both corporations and individuals, it would also eliminate the death tax and reorganize the Internal Revenue Service into three independent units.

In a June 28 letter to Brady, Diane VanDe Hei, CEO of the Association of Metropolitan Water Agencies, said that nearly $40 billion in tax-exempt water and sewer debt was issued in 2012 alone to fund water-related infrastructure. Should muni interest become subject to a tax, Van DeHei said investors would charge higher interest rates to offset the new expenses, leading to what would be "billions of dollars" of additional financing costs for municipalities.

"AMWA appreciates that the 'A Better Way' tax reform blueprint … does not explicitly call for the reduction or elimination of tax-exempt municipal bond interest," Van DeHei wrote. "But the blueprint also lacks an outright pledge to maintain tax-exempt interest on municipal bonds, and worryingly suggests that interest income in general could be taxed at the same 'reduced' rates as other investments."

The House Ways and Means Committee, which is still reviewing written responses to the blueprint, has not yet made comments available to the public. A spokeswoman declined to cite how many have been received.

In a June 24 op-ed in The Wall Street Journal, Brady said, "House Republicans will spend the coming months listening to and incorporating feedback from our constituents."

The Securities Industry and Financial Markets Association in June commended lawmakers for aiming to reform the tax code, and said it planned on submitting comments to the House Ways and Means Committee. SIFMA spokeswoman Carol Danko said Wednesday that the organization has yet to do so.

The Tax Foundation, the think tank that tracks tax issues, released a report earlier this month suggesting lawmakers consider limiting, reforming or eliminating the current muni exclusion, claiming it is inefficient and mostly benefits the wealthy. Muni advocates have blasted the report, disagreeing with its findings.
