THE BOND BUYER

Municipal market gains a sympathetic ear on tax policy

By

Brian Tumulty

Published

December 28, 2018, 9:23am EST

WASHINGTON – The legislative outlook for the tax treatment of municipal bonds is brighter in 2019 than a year ago with a strong supporter of municipal bonds ascending to the chairmanship of the Ways and Means Committee as part of the new Democratic majority.

Rep. Richard Neal, D-Mass., begins serving as chair the panel that formulates federal tax policy with a pledge to ask mayors, governors and other municipal market advocates to testify at hearings early in the year on the impact of the 2017 Tax Cuts and Jobs Act.

That legislation was a blow to the municipal bond market because of the termination of advance refundings. Restoration of them is a high legislative priority of the Government Finance Officers Association, the National Association of Bond Lawyers and the Securities Industry and Financial Markets Association, among others.

Republican Rep. Randy Hultgren of Illinois, who was the sponsor of a bill to restore advance refundings, lost his seat in the November election.

NABL President Dee Wisor, an attorney at Butler Snow in Denver, said his organization is working with GFOA to find a new sponsor for the advance refundings bill.

GFOA also had teamed up with state and local groups to fight elimination of the $10,000 cap on the federal income tax deduction for state and local taxes.

Democratic Rep. Bill Pascrell, a former mayor of Paterson, N.J., and a member of the Ways and Means Committee, said he will sponsor a proposal to fully restore the SALT deduction that would be fully paid for from the offsetting revenue of raising the corporate tax rate to 23% or 24% from 21%.

“We want to do everything we can to pay for it,” said Pascrell. “It’s a powerful deduction in states that are high tax states. Because they are high density states they’ve got different needs than if you are living in Wyoming or North Dakota.”

Senate Republicans, however, are unlikely to support a partial rollback of the reduction of the corporate tax rate they enacted in December 2017.

A tax provision on the wish list of the Bond Dealers of America is an increase in the limit for bank qualified loans to $30 million from $10 million, said Brett Bolton, BDA’s vice president of federal legislative and regulatory policy.

Muni groups are confident that at the very least their requests will get public consideration.

Neal said on the House floor Dec. 20 during debate on tax policy, “There will be hearings and there will be witnesses and it will be done in daylight to make sure there is an opportunity for all to be heard, including our Republican friends.”

That statement was made during floor debate on a catchall package of tax measures pushed by Neal’s predecessor, Rep. Kevin Brady, R-Texas, that failed to gain Senate consideration.

One those failed provisions was a tax fix for bond-financed multifamily housing projects that have a residency preference for military veterans.

Neal didn’t mention the muni provision, but he lectured Republicans for failing to work in a bipartisan way on many year-end tax measures Democrats support. He criticized them for packaging the provisions with poison pills, such as a measure to allow members of the clergy make political endorsements from the pulpit without endangering the tax-exempt status of churches and synagogues, and for not including revenue offsets.

The muni provision was noncontroversial and the cost of it received only a non-consequential asterisk in the nonpartisan Congressional Budget Office analysis.

About half of the multifamily housing units built nationally that use the federal 4% Low Income Housing Tax Credit are financed with tax-exempt private activity bonds. The other half use a 9% federal tax credit that does not allow PAB financing.

Federal law doesn’t explicitly say that veterans qualify for a special needs exception to the public use rules governing the tax-exemption for multifamily PABs.

Treasury officials have indicated they don't want to issue a private letter ruling to clear up the problem, which leaves the solution to be either through congressional legislation or published guidance such as a revenue notice.

Also caught up in the year-end impasse on tax measures was aid for disaster victims through tax breaks and federal aid to communities where those disasters occurred. Localities often count on that aid to get back to business as usual and to help ward off adverse credit effects.

Neal said he "will try very quickly to address many of these same issues" in the new Congress.

Wisor, the NABL president, isn't optimistic much tax legislation will move in 2019 given that Congress will be divided with Republicans in control of the Senate.

"I'm not sure that that's going to be anything other than maybe some political theater so they can say they are providing some transparency because it seems hard to get 60 votes in the Senate to undo anything in the bill," Wisor said.

"I do think that infrastructure is a place where there's an opportunity for some bipartisanship," Wisor added. "The people we have been talking to on the Hill seem to agree with that. So maybe there's an opportunity for some narrow tax policy in the context of an infrastructure bill. For example, expanding private activity bonds.''

Ken Bentsen, president and CEO of SIFMA, similarly predicted that infrastructure can be an area of bipartisan agreement, noting there's an impetus to do it because the current federal highway bill expires in 2020.

"We're not anticipating a major tax bill," Bentsen said. "At this point in time historically you normally wouldn't see one so soon after a prior tax bill. However, we are always diligent about protecting the tax exempt status of municipal bonds and that remains our top tax priority."

SIFMA officials foresee a revival of federal direct-pay bonds as a possible element of an infrastructure bill although they might not be called Build America Bonds as they were in the recent past.

SIFMA and NABL have told congressional policymakers that any new form of direct pay bonds will need to be exempt from across-the-board budget cuts under a sequester to attract market interest.

They also have advised that existing BABs, many of which are non-callable, should also be exempted from sequester cuts.

“The point we made was that given what happened on sequestration it’s probably not going to enjoy much support from local governments if it is something that is subject to sequestration,” said Wisor. “And so that will be part of the policy debate. Might you make it a like tax refund for an individual which is not subject to sequestration? That will be a question to be answered.”

SIFMA and NABL both favor eliminating volume caps for transportation and infrastructure related PABs.

Each state has a volume cap that applies to certain categories of PABs. In addition, there’s a $15 billion nationwide cap on highway related PABs that’s subject to allocations approved by the U.S. Department of Transportation. Muni groups want those caps eliminated.

Democratic Rep. Earl Blumenauer of Oregon said there’s “an excellent chance” the $15 billion cap will be raised, describing it as “a relatively easy lift.”

Rep. Brian Higgins, D-N.Y., withheld support for House Democratic Leader Nancy Pelosi to serve as speaker until she promised to make a best effort to enact infrastructure legislation and an expansion of Medicare eligibility to people between the ages of 50 and 64.

“It’s an agreement in principle to make a good-faith effort to get those two issues done in the 116th Congress,” Higgins said in an interview.

Higgins, an eight term House member from Buffalo, said too much emphasis has been placed on economic need such as deteriorating bridges and not enough has been placed on the benefits of infrastructure investment through job creation and economic growth.

“Unlike tax cuts, infrastructure does in effect pay for itself,” Higgins said. “For every dollar you invest, you get about $1.60 in economic growth.” Spending $1 trillion over five years would produce 11.5 million jobs and add 1-1/2% to 2% in annual economic growth annually, he said.

However, the initial post-election optimism about the prospects for bipartisan agreement on tax provisions to encourage infrastructure construction has been tempered in recent weeks by President Trump’s demand that any package should include funding for a wall on the southern border.

And Senate Democratic Minority Leader Chuck Schumer of New York has said Democrats want any infrastructure package to include provisions for addressing climate change.

How much of those demands are simply political messaging is unclear.