Policy Update – Tax Reform Bill Heads to Conference

Lewis-Burke Associates LLC – December 4, 2017

In the early hours of December 2, the Senate passed their version of the *Tax Cuts and Jobs Act* along a party-line vote of 51-49. Senator Bob Corker (R-TN) joined every Senate Democrat in voting against the measure.

The final Senate bill approved Friday night removed a provision included in earlier Senate versions that would have treated name and logo royalties as unrelated business income (UBI). The final bill also included an endowment excise tax provision on certain *private* universities with assets above $500,000 per full-time student. This is a higher threshold than previous versions and the House bill. Of note, the Senate bill retained the provision that called for separate calculations of UBI activity, the repeal of charitable deduction for athletic seat licenses, a new excise tax on executive compensation, and the repeal of tax benefits for advance refunding bonds.

For the upcoming bill conference, the House will appoint conferees on December 4, and Senator Majority Leader McConnell (R-KY) said he would appoint conferees sometime this week; however, informal negotiations have already started between the chambers. It is believed that congressional leaders will strive to get the conference and final bill completed within the next two weeks.

Conferees will have to iron out significant differences in the packages that have passed the respective legislative bodies. These include differences over the permanence of individual tax cuts, the number of tax brackets, the treatment of "pass-through" income, the maintenance of the estate tax, and the repeal of the *Affordable Care Act* individual mandate penalty (present in the Senate version but absent in the House version), among other differences. Both versions include a deduction for property taxes, capped at $10,000, but eliminate the deduction for state and local income tax, a large sticking point for Republican members from high-tax states. Several of these members voted against the tax bill that passed the House due to concerns about the state and local tax deduction. Additionally, any package would have to be compliant with Senate budget rules, a factor that would favor the Senate version.

Conferees will now look to craft a package that can pass both chambers, meaning provisions from both the House and Senate versions are in play. Institutions and associations have been active in ensuring that provisions such as the tax on tuition waivers were not included in the Senate version, and will want to continue these advocacy efforts.

Below are provisions in both the House and Senate bills that would significantly impact institutions of higher education and other tax-exempt nonprofits.

**Education benefits and credits**
*Where they differ:* The House bill proposes the elimination of the Hope Scholarship and Lifetime Learning Credits and would create a modified American Opportunity Tax Credit (AOTC). The House
version would also eliminate Section 117(d) which allows institutions to provide tuition reduction/waivers to employees and their dependents, and under 117(d)(5), to graduate students. This would create a new tax liability for institutions and students. It would also eliminate Section 127, which allows tax-free treatment of employer-provided education assistance.

The Senate version maintains the deduction for student loan interest and does not make changes to student education tax credits. Both bills would expand Section 529 college savings accounts to cover K-12 expenses of up to $10,000 per year. Additionally, the Senate proposal would allow savings to be used for dual enrollment in an institution of higher education. Significantly, the Senate version maintains workforce educational benefits eliminated in the House proposal, including Section 117(d) and Section 127.

**Main impacts:** The House version would harm part-time students, graduate students, and life-time learners. It would create a new tax on many graduate students, in some cases doubling their tax liability. Students would also lose the ability to deduct student loan interest payments. The Senate version maintains many of the current education benefits.

**Charitable contributions**

*Where they differ:* While both versions propose expanding the standard deduction, the House version would expand the deduction to $12,200 for individuals and $24,400 for married couples filing jointly. The Senate version expands the deduction to $12,000 and $24,000 respectively. The House version expands the exemption for the estate tax, but eventually phases it out completely. While the Senate version expands the estate tax exemption, it maintains the tax. The ability to deduct 80 percent of the amount paid for the right to purchase tickets for athletic events is eliminated in both bills. Both versions also increase the limit on cash contributions to qualified organizations from 50% to 60% of taxable income.

*Main impacts:* The congressional Joint Committee on Taxation (JCT), has estimated that as a result of these changes, the number of filers claiming the charitable deduction will drop from roughly 40 million to 9 million. This will lead to an estimated $100 billion less in charitable giving over the next decade.

**Unrelated Business Income Tax (UBIT)**

*Where they differ:* The House version clarifies that the exclusion of income from fundamental research for tax-exempt organizations applies only when the results are freely available to the public. The Senate version initially proposed to treat income from licensing of any name or logo of tax-exempt organizations as an unrelated trade or business income, but that provision was removed in the final Senate negotiations. However, the Senate bill would require that unrelated business income be separately computed for each trade or business activity and includes a provision that prohibits losses from one unrelated activity to offset gains by another unrelated trade or business activity. Additionally, there are new limitations on the use of net operating loss deductions in both bills.

*Main impacts:* The separate calculation of unrelated business activities will create additional tax and administrative burdens for institutions and nonprofit organizations.

**Excise tax based on investment income of private colleges and universities**

*Where they differ:* The House and Senate versions both contain a provision that would subject certain private colleges and universities to a 1.4 percent excise tax on net investment income. In the House bill, the provision would only apply to private colleges and universities that have at least 500 students and
assets of at least $250,000 per full-time student. The Senate modified this provision to only apply to certain private institutions with assets of at least $500,000 per full-time student. Public institutions would not be subject to the provision.

*Main impacts:* Endowments give schools the ability to fund undergraduate scholarships, student services, research, and patient care and any tax would divert resources from serving the campus community. Including a tax on educational institutions sets an unwelcome precedent in the tax code.

### Private activity bonds (PABs) and advance refunding bonds

*Where they differ:* The House version would eliminate private activity bonds while both bills would eliminate advance refunding bonds.

*Main impacts:* Private activity bonds are often used by nonprofits to finance capital projects like classrooms, lecture halls, and energy plants. The ability to access PABs and advance refunding bonds is a critical financing tool for nonprofits.

### Other Areas of Concern

The House version eliminates the historic rehabilitation tax credit, and the Senate version would reduce the expenses eligible for the credit. Both versions would subject tax-exempt organizations to a 20 percent excise tax on executive compensation that is in excess of $1 million paid to any of its five highest paid employees. The House version also includes a change to the exclusion of housing benefits from tax liability. Further, the House bill would change the “Johnson Amendment,” which would permit 501(c)(3) organizations to endorse or oppose political candidates.

### Final Thoughts

The House and Senate conference is expected to move quickly even though obstacles remain. A final bill is likely to be sent to the president by end of this month as there is tremendous pressure for congressional Republicans to finish tax reform this year. While there are indications that Senate Republicans do not favor targeting education credits and benefits as proposed in the House bill, those provisions, like the others noted above, are still currently on the table for negotiations. Affected institutions, students, and research organizations should continue outreach to their Members of Congress in both the Senate and the House, as any of these provisions may be included in a final package.

### Sources and Additional Information:

- The House passed H.R. 1, the *Tax Cuts and Jobs Act* is viewable at [https://www.congress.gov/115/bills/hr1/BILLS-115hr1pcs.pdf](https://www.congress.gov/115/bills/hr1/BILLS-115hr1pcs.pdf).
- Details on the final Senate managers package for the Senate’s *Tax Cuts and Jobs Act* and approved amendments can be found at [https://www.finance.senate.gov/committees/finance-committee-announces-improvements-to-senate-tax-bill](https://www.finance.senate.gov/committees/finance-committee-announces-improvements-to-senate-tax-bill).
- The higher education associations’ comparison chart of provisions of interest in the House and Senate bills can be found at [http://www.acenet.edu/news-room/Documents/Tax-Reform-Bill-Comparison.pdf](http://www.acenet.edu/news-room/Documents/Tax-Reform-Bill-Comparison.pdf).