ORRIN G. HATCH, UTAH, CHAIRMAN

CHUCK GRASSLEY, IOWA
MIKE CRAPO, IDAHO
PAT ROBERTS, KANSAS
MICHAEL B. ENZI, WYOMING
JOHN CORNYN, TEXAS
JOHN THUNE, SOUTH DAKOTA
RICHARD BURR, NORTH CAROLINA
JOHNNY ISAKSON, GEORGIA
ROB PORTMAN, OHIO
PATRICK J. TOOMEY, PENNSYLVANIA
DEAN HELLER, NEVADA
TIM SCOTT, SOUTH CAROLINA
BILL CASSIDY, LOUISIANA

RON WYDEN, OREGON
DEBBIE STABENOW, MICHIGAN
MARIA CANTWELL, WASHINGTON
BILL NELSON, FLORIDA
ROBERT MENENDEZ, NEW JERSEY
THOMAS R. CARPER, DELAWARE
BENJAMIN L. CARDIN, MARYLAND
SHERROD BROWN, OHIO
MICHAEL F. BENNET, COLORADO
ROBERT P. CASEY, JR., PENNSYLVANIA
MARK R. WARNER, VIRGINIA
CLAIRE McCASKILL, MISSOURI

A. JAY KHOSLA, STAFF DIRECTOR
JOSHUA SHEINKMAN, DEMOCRATIC STAFF DIRECTOR

United States Senate

COMMITTEE ON FINANCE

WASHINGTON, DC 20510–6200

December 18, 2017

The Honorable Bob Corker
425 Senate Dirksen Office Building
Washington, D.C. 20510

Dear Chairman Corker,

Thank you for your letter dated yesterday.

I am disgusted by press reports that have distorted one particular aspect of the conference agreement on H.R.1, the Tax Cuts and Jobs Act. The reports have focused on the final version of the 20 percent pass-through deduction, the proposed new Section 199A. As the author of this provision and the vice chairman of the conference committee, I can speak with authority about the process by which the conference committee reached its final position.

There are two false assertions contained in these reports, and I would like to correct the record on both.

First, some have asserted that a new provision was crafted for real estate developers and was "air-dropped" into the conference agreement. Second, reports have implied that you had some role in advocating for or negotiating the inclusion of this provision.

Both assertions are categorically false. With respect to the second, I am unaware of any attempt by you or your staff to contact anyone on the conference committee regarding this provision or any related policy matter. To the contrary, virtually all the concerns you had raised in the past about the treatment of pass-through businesses in tax reform were to voice skepticism about the generosity of various proposals under consideration.

The first claim – that a new pass-through proposal was created out of whole cloth and inserted into the conference report – is an irresponsible and partisan assertion that is belied by the facts. For more than a year, tax-writers in the House and Senate have worked to craft legislation that not only provided relief for "C" corporations, but also delivered equitable treatment for pass-through businesses. Though the two chambers came at this issue from different angles, our goal was the same: To provide tax relief to pass-through businesses at a level similar to that provided to regular "C" corporations. This policy goal was confirmed in the *Unified Framework for Fixing Our Broken Tax Code*, which provided in part:

> *"TAX RATE STRUCTURE FOR SMALL BUSINESSES The framework limits the maximum tax rate applied to the business income of small and family owned businesses conducted as sole proprietorships, partnerships and S corporations to 25%. The framework contemplates that the committees will adopt measures to prevent the re-characterization of personal income into business income to prevent wealthy individuals from avoiding the top personal tax rate."*

The House Ways Means Committee and the Senate Finance Committee achieved this mutual goal by different means. Section 1004 of the House bill provided a special tax rate for pass-through income and

included a "prove-out" option for capital-intensive businesses. Chairman Brady unveiled this approach on November 2nd, more than six weeks ago.

The Senate took a different approach, achieving the intended rate relief through a deduction patterned after current law Section 199. We also included measures to ensure that compensation could not be easily gamed into business income in order to qualify for the deduction. Similar to Section 199, the deduction in the Senate bill excluded compensation and guarantee payments to owners and was limited to 50 percent of compensation paid to employees, with an exception for small pass-through businesses, including service providers. The Senate bill did not include a prove-out option for capital-intensive businesses like the one contained in the House bill.

The Joint Committee on Taxation ("JCT"), the non-partisan congressional scorekeeper for tax legislation, released a side-by-side summary of the two bills for conferees. That summary, dated December 7, 2017 and available on JCT's website (JCX 64-17), described the House position in part:

> "In the case of a capital-intensive business, a taxpayer may "prove out" a capital percentage by electing the application of an increased percentage for the taxable year it is made and each of the next four taxable years. The applicable percentage is determined by dividing (1) the specified return on capital for the activity for the taxable year, by (2) the taxpayer's net business income derived from that activity for that taxable year."

It takes a great deal of imagination – and likely no small amount of partisanship – to argue that a provision that has been public for over a month, debated on the floor of the House of Representatives, included in a House-passed bill, and identified by JCT as an issue requiring a compromise between conferees is somehow a covert and last-minute addition to the conference report.

I have sat on a number conference committees, too numerous to remember. In each case, conferees have come into the conference expecting to achieve their chamber's position or negotiate a reasonable compromise. This conference committee was no exception. The House entered the conference with an interest in preserving, in some form, the prove-out alternative as an option for capital-intensive taxpayers. Through several rounds of negotiations, the House secured a version of their proposal that was consistent with the overall structure of the compromise.

The prove-out alternative included in the conference report was derived from the House provision and is the product of a negotiation between the House and Senate tax-writing committees. It is that simple.

If you have any further questions, please feel free to contact me.

Very Truly Yours,

Orrin G. Hatch,
Chairman, Senate Finance Committee

Cc: The Honorable Kevin Brady, Chairman, House Committee on Ways and Means
The Honorable Mitch McConnell, Majority Leader, United States Senate