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Washington Commentary

Biden's Tax Policy – What's Reconciliation Got to Do With It?

In a normal election year, a president's and their challenger's economic and tax policy vision is a primary barometer of their electability.

But 2020 is no normal election year. The country is recovering, reopening, and reexamining the appropriate policies to respond to a 100-year pandemic juxtaposed with a 360-degree examination of its moral fiber in response to police brutality and racism. Those biometric pressure points will weigh heavily on voters but maybe more so on former Vice President Biden who will need to assertively counter President Trump with his own economic vision when the country is clamoring for hope.

President Trump achieved what many thought impossible when, in a Republican-held Congress, he marshalled through the Tax Cuts and Jobs Act (TCJA) in December 2017. TCJA crystalized the Republican economic platform and achieved long sought Republican objectives to reduce both the individual and corporate tax rates, as well as simplifying and modernizing the international tax code to promote competitiveness. This was the country's first major overhaul of the tax code since 1986 and was supposed to be the Republican's greeting card for a generation of voters making the case for why their economic vision was best.

Biden's Proposed Tax Policy Highlights

Increase the top individual tax rate from 37% to 39.6% for those with taxable incomes over $400,000
Tax long-term capital gains and qualified dividends at 39.6% on income above $1 million and eliminate the step-up basis
Imposes the 12.4% Social Security tax on income earned above $400,000 (evenly split between employers and employees), which would create a "donut hole" in the current payroll tax where wages between $137,000, the current wage cap, and $400,000 are not taxed
Raise the corporate tax rate from 21% to 28%
Create a 15% minimum corporate tax rate for companies with net incomes over $100 million

TCJA was made possible by a seldom used and little understood piece of legislation from 1974, the Budget and Impoundment Control Act (ICA). The powers of the ICA are numerous. Among other things, it created a legislative process called Reconciliation that expedites the passage of certain budgetary legislation in the United States Senate without the threat of filibusters and extraneous non-germane amendments, allowing for the passage of bills with a simple majority. The Reconciliation directives authorize Committees to come up with mandatory cuts and/or changes in the law that will facilitate such cuts. It is a vehicle that has been used to implement major changes including tax, infrastructure, energy and health related provisions including the Economic Growth and Tax Relief Reconciliation Act of 2001 ("Bush tax cuts") and the Health Care and Education Reconciliation Act of 2010 (amended Obamacare). These powers allowed Republicans to pass the TCJA with a simple majority along partisan lines, and Democrats could look to run a similar playbook next year if they maintain control of the House and take the Senate and White House.

How Biden distinguishes his economic vision could carve a path to victory or alienate voters. With record unemployment numbers not seen since the Great Depression, voters want answers and they need jobs now. There will be tremendous pressure from not only the poles of the Democratic base but from congressional members and staffers who still have heartburn from the partisan-push behind TCJA to unravel it. Though Biden has said he does not want to undo all of TCJA, more likely than not, Democrats will seek to use the same budgetary maneuvering to dismantle TCJA (and achieve other policy goals) and pass their vision of tax reform. But achieving even partial tax reform will not be easy in a closely divided Senate and it will have to compete with other priorities.

The former vice president recently characterized his tax vision: "My tax policy is based on a simple proposition…which is, stop rewarding wealth and start rewarding work a little bit." For this, Biden might rely heavily on the famous tax adage of former Louisiana Senator Billy Long who, when trying to build support for tax increases, said, "Don't tax you, don't tax me, tax that man behind the tree." Biden himself has pledged that no voter making under $400,000 will see a tax increase. According to the Tax Foundation, the Biden tax plan would lead to 7.8% less after-tax income for the top 1%, 1.1% lower after-tax for the top 5%, and around 0.6% less after-tax income for the other income quintiles in 2030.

While Biden has outlined several of his tax and economic visions including expanding the Earned Income Tax Credit and Small Business Retirement Tax Credit and reforming childcare tax credits, Congress will largely have the responsibility to bring his (and his voters') aspirations to reality. Presidents campaign, Congress legislates. If Democrats control all of Washington, there will be tremendous pressure to deliver on many expensive but politically necessary societal objectives – climate change, infrastructure, social and educational reforms. All of these will likely need to be paid for via budgetary maneuvers that congressional leadership will have to wrestle with unless the Senate takes the historic step and ends the filibuster. Changing the Senate rules to end the filibuster would create additional legislative paths but would create an internal debate in the chamber between institutionalists and newer members that are frustrated by the dearth of legislating of late.

Just as Republicans had to persuade fiscal hawks in their ranks that passing tax reform was an opportunity they could not squander, Democrats will have to do the same with their moderates when it comes to voting for a budget to clear a path for rewriting the tax code. This will not be easy. One of the first steps in this process of reforming the tax code would be led by potential Senate Budget Committee Chairman Bernie Sanders (D-Vermont) as he would need to advance a budget resolution through his committee and the floor. It is not a stretch to say Senator Sanders's economic and tax priorities fall outside of the umbrella of most of his peers (only fellow Vermont Senator Patrick Leahy (D) endorsed his presidential campaign). This will make passing a budget that meets his policy compass and his party's desires an incredible challenge.

Moderate Democratic senators from purple and battleground states might gravitate towards the middle of the political spectrum and not look too keenly on increasing taxes on individuals (and corporations) when the economy is returning from a recession. There will be tremendous pressure on senators like Senators Kyrsten Sinema (D-Arizona), Joe Manchin (D-West Virginia), John Tester (D-Montana), Chris Coons (D-Delaware), and others to not support a budget that calls for tax increases. There will be equal pressure to find new revenue streams to support much sought-after Democratic policy objectives. And this calculus on getting to the necessary 50 votes for reconciliation does not include forcing potential freshman senators in purple states like North Carolina, Arizona, Colorado and/or Iowa to vote for a tax increase in their first year in office.

The challenges to passing a budget in the House will be equally hard. Democratic leadership will have to overcome a boisterous progressive bunch while pulling along large pockets of moderate Democrats (over 100 members in the pro-business New Democrat Coalition and 26 in the centrist Blue Dog Coalition) by selling a budget as a necessary step to achieve long sought policy goals. But remember, in 2019, House Democrats failed to advance their own budget when members fought over hot-button provisions like the Green New Deal and Medicare for All.

As the country inches towards November, the details of Biden's tax vision will come under greater scrutiny as will President Trump's economic restart efforts. These are critical evaluation periods for voters but it's important to recognize that wholesale tax reform is not easy – it has only happened once in nearly 30 years despite the ability for Congress to move tax priorities via a simple majority. In 2017 the stars were aligned for Republicans and unless Democrats control all of Washington, Biden's economic and tax policies will only be remembered as talking points in an election.

Invesco US Government Affairs

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Andy Blocker serves as Head of US Government Affairs for Invesco. In this role, he drives Invesco's legislative and regulatory advocacy initiatives with policymakers, engages with clients and opinion leaders on public policy developments, and seeks to maximize the company's political footprint. Previously, Andy served as executive vice president of public policy and advocacy for the Securities Industry & Financial Markets Association, where he led a team engaging lawmakers on international, federal and state issues impacting the financial services industry. Andy spent five years as managing director for the US Office of Public Policy for UBS. He also served as vice president of government relations for the New York Stock Exchange, as managing director of government and international affairs for American Airlines, and for the White House as special assistant to the president for legislative affairs.

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