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INSIGHT: TTC/EY Tax Policy Business Barometer: Views on Federal Tax Policy—December 2018

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The Tax Council (TTC) and Ernst & Young LLP introduced the Tax Reform Business Barometer in 2013 to measure the business community's perceptions on the prospects for federal business tax reform and other key policy issues. With the enactment of the Tax Cuts and Jobs Act (TCJA) in December 2017, TTC and Ernst & Young LLP developed the Tax Policy Business Barometer (Barometer) to measure the perceptions of the business community on the implementation of the TCJA and a broad set of other policy issues.

This 17th Barometer included questions on the TCJA, international tax reform, trade policy, infrastructure, and the federal government's long-term fiscal imbalance. It tracked the views reported from Dec. 10–19, 2018. Ninety-one leading U.S. tax executives and practitioners completed the December Barometer. Results are based on an online survey conducted by EY's Quantitative Economics and Statistics (QUEST) practice.

KEY RESULTS

TCJA implementation

- **TCJA's temporary provisions will be extended:** On average, respondents believe there is a 71 percent likelihood that the major temporary TCJA provisions will be extended at some point.

- **Individual tax provisions are the most likely to be extended:** Of those who believe major TCJA provisions will be extended, more than three-quarters (76 percent) believe that individual tax rates will be extended. Fifty-eight percent believe the 20 percent deduction for pass-through income will be extended.

- **More stringent earnings before income tax (EBIT)-based interest limitation likely to take effect as scheduled in 2022:** 80 percent of respondents believe it is at least somewhat likely the EBIT-based interest limitation will go into effect in 2022.

Impact of international tax changes

- **TCJA's Global Intangible Low-Taxed Income (GILTI) provision will affect companies' or industries' foreign earnings, such that it limits the benefit from the new dividend exemption/territorial system for most organizations:** 84 percent of respondents believe the GILTI provision will have a moderate or large impact on their foreign earnings that will effectively limit the benefit from the dividend exemption/territorial system.

- **TCJA thought to have little impact on incentives for deciding where to locate production and jobs:** Of those respondents who are affected by the law's international tax provisions, 51 percent believe the TCJA had no impact on the incentive for moving production and jobs abroad, 39 percent believe the TCJA decreased the incentive, and 10 percent believe it increased the incentive.

Tariffs and trade policy

- **A trade war is likely to cause a recession:** 68 percent of respondents believe that a trade war is at least somewhat likely to push the U.S. economy into a recession.

- **Trade frictions likely to continue in the new year and beyond:** Most respondents believe that the current trade frictions and increased tariffs between the U.S. and its major trading partners will not begin to de-escalate until 2021.

- **Respondents believe the Trump administration's approach to China will be successful:** 63 percent of respondents think that it is at least somewhat likely that the administration's approach to trade policy and tariffs will succeed in getting China to reform its trade practices relating to intellectual property and forced technology transfers. The remaining 37 percent of respondents think the current approach is not very likely or not likely at all to succeed.

- **Modeling tariffs important for some:** Thirty-eight percent of respondents report doing some or extensive modeling on the impact of tariffs on their company, industry, or market, while the remainder report doing no modeling on the issue.

Infrastructure

- **Deteriorating infrastructure is a major problem for businesses:** 85 percent of respondents believe deteriorating infrastructure poses a problem for their business or industry.

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■ **Respondents think increasing the gasoline tax is a good way to pay for infrastructure improvements:** When asked to pick top funding choices, respondents overwhelmingly prefer a gasoline tax (82 percent) to other sources of federal funding for infrastructure projects, followed by a carbon tax (55 percent).

Federal government's long-term fiscal outlook

■ **No consensus on whether the federal government will address its long-term fiscal imbalance:** Respondents believe, on average, that there is a 54 percent likelihood that Congress will not enact any legislation within the next five years to address the federal government's long-term fiscal imbalance.

■ **Increasing corporate income taxes is the most likely approach Congress will take to reduce the deficit:** 76 percent of respondents cited increasing corporate income taxes as one of the top three most likely approaches Congress will take to reduce the federal government's long-term fiscal imbalance.

MOVING FORWARD UNDER THE TCJA

The December 2018 Barometer asked several questions on the likelihood of enactment of technical corrections legislation and legislation to make various sunsetting provisions permanent, as well as the likelihood of future revenue-raising provisions going fully into force.

Extending sunsetting TCJA provisions

The TCJA contains a number of provisions that will sunset or be phased out by 2022. These include the reduced individual tax rates, the 20 percent qualified pass-through income deduction, 100 percent bonus depreciation, and changes to the individual tax base. In general, respondents believe these provisions will eventually be extended, but not within the next several years:

■ Respondents believe, on average, that there is a 71 percent likelihood that the major expiring provisions of the TCJA will be extended. However, on average, respondents believe there is a 27 percent likelihood that major expiring provisions of the TCJA will not be made permanent until 2023 or later. Respondents give a 29 percent likelihood that the major TCJA provisions will not be extended at all.

■ Respondents give, on average, a 6 percent likelihood that legislation making these provisions permanent will be enacted in 2019, an 11 percent likelihood of enactment in 2020, a 13 percent likelihood of enactment in 2021, and a 14 percent likelihood of enactment in 2022.

When do business tax professionals think TCJA's sunsetting provisions will be extended?

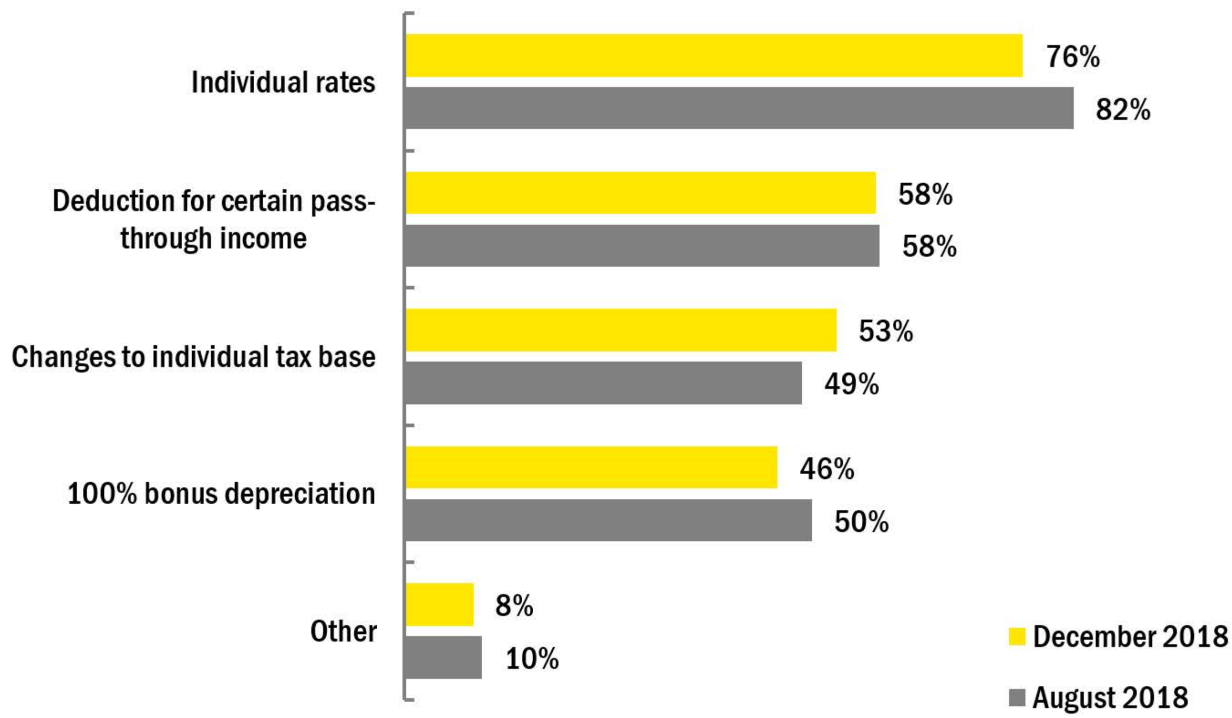
Expected year of TCJA extension	2018	2019	2020	2021	2022	After the next four years*	TCJA not extended
December Barometer	–	6%	11%	13%	14%	27%	29%
August Barometer	8%	14%	11%	11%	–	28%	27%

December and August 2018 Barometers. *Answer option is phrased as the fifth year from the current year ''. . .or beyond.'' For example, the August 2018 Barometer answer choice was ''2022 or beyond.'' Percentages reflect average likelihood.

Note: Percentages may not sum to 100 percent due to rounding.

Of the respondents who believe major provisions of the TCJA will be extended, the consensus is that individual rate cuts are likely to be made permanent (76 percent). More than half (58 percent) of respondents believe that the deduction for certain pass-through income is likely to be made permanent.

Which provisions do business tax professionals deem most likely to be made permanent?



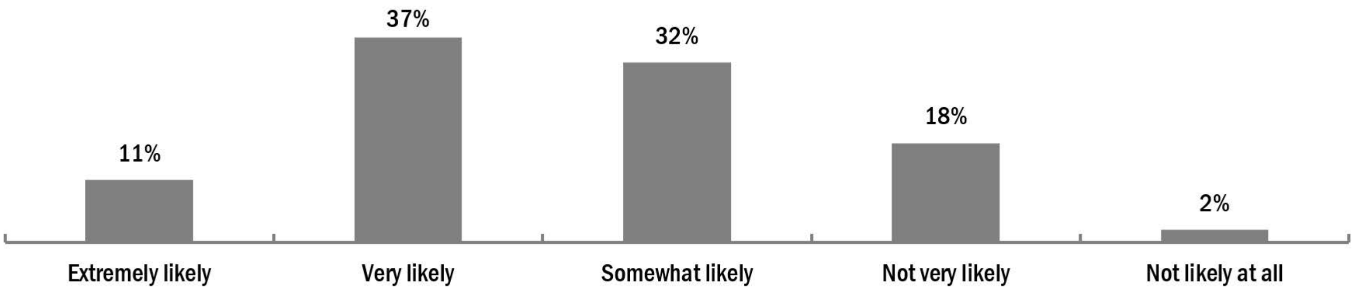
Respondents are about evenly split on the fate of bonus depreciation and the changes to the individual tax base (e.g., the limitation on the deduction of state and local taxes), with 46 percent and 53 percent, respec-tively, thinking those provisions are likely to be extended.

Will the EBIT-based interest expense limitation and amortization of certain research and experimentation (R&E) expenditures fully go into force as scheduled (beginning of 2022)?

Two major revenue-raising provisions of the TCJA, the EBIT-based interest expense limitation and the amortization of certain R&E expenditures, are not scheduled to fully go into force until the beginning of 2022. According to estimates from the Joint Committee on Taxation (JCT), the EBIT-based interest expense limitation and amortization of certain R&E expenditures are expected to raise $188.1 billion and $119.7 billion, respectively, between 2022 and 2027.

Most respondents (80 percent) believe that it is at least somewhat likely the EBIT-based interest expense limitation will fully go into force in 2022. Eleven percent believe it is extremely likely, 37 percent believe it is very likely, and 32 percent believe it is somewhat likely that this provision will fully go into force as scheduled. Only 18 percent believe it is not very likely and 2 percent believe it is not likely at all to fully go into force as scheduled.

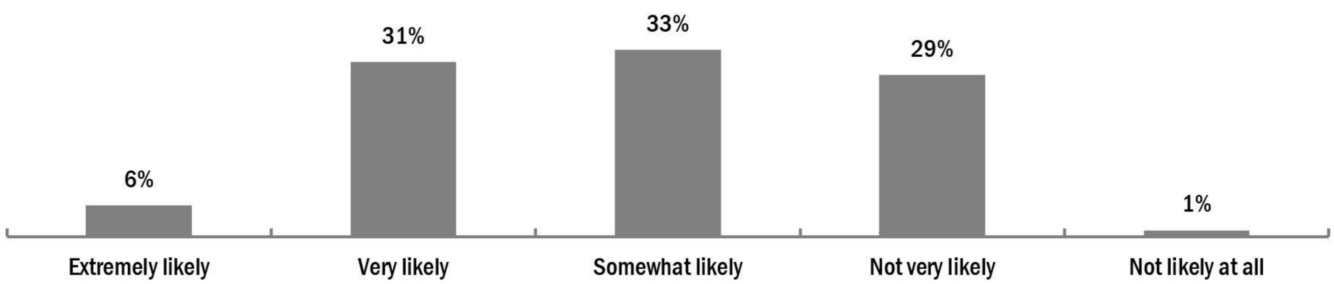
Likelihood that EBIT-based interest expense limitation will fully go into force at the beginning of 2022



Note: Percentages may not sum to 100% due to rounding.

Seventy percent of respondents think it is at least somewhat likely that the TCJA provision requiring amortization of certain R&E expenditures will go into effect as scheduled at the beginning of 2022. Only 6 per-cent believe it is extremely likely the provision will go fully into force, while 31 percent and 33 percent believe it is very or somewhat likely, respectively. Slightly under one-third (29 percent) believe it is not very likely that the provision will fully go into force and only 1 per-cent believe it is not likely at all.

Likelihood that amortization of certain R&E expenditures goes fully into force at the beginning of 2022



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Impact of international tax changes

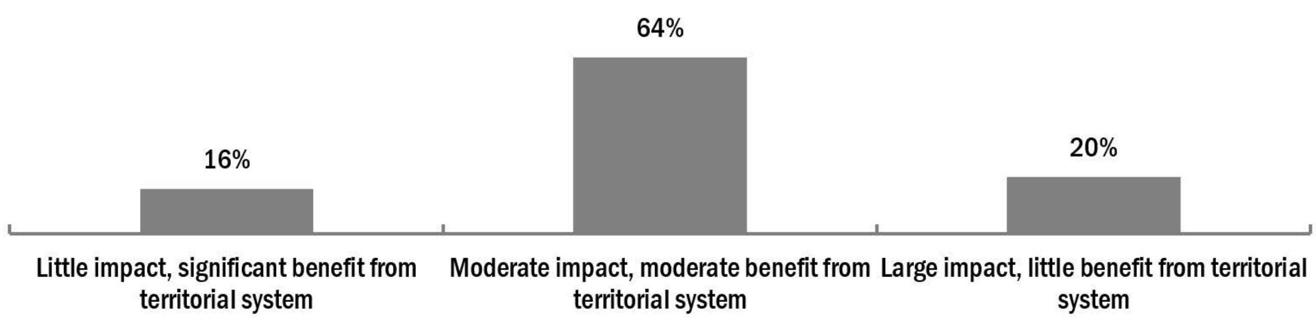
The TCJA included a number of international tax provisions that expand and change the tax base. This Barometer included a question on the impact of the new GILTI provision and dividend exemption/territorial system and on how the TCJA may have affected the incentive for where companies or industries locate production and jobs.

Impact of GILTI may offset the benefit of new dividend exemption/territorial system

Of respondents affected by the TCJA's GILTI provisions, 84 percent view it as having a moderate or large impact on their company's or industry's foreign earnings that will in effect limit their benefit from the dividend exemption/territorial system.

- Sixty-four percent say the TCJA's GILTI provisions will have a moderate impact on their company's or industry's foreign earnings, such that their company's or industry's foreign income benefits moderately from the new dividend exemption/territorial system.
- Twenty percent report that GILTI will have a large impact on their company's or industry's foreign earnings, such that their company's or industry's foreign income will receive little benefit from the new dividend exemption/territorial system, including the GILTI tax.
- Sixteen percent believe the GILTI provisions will have little impact on their company's or industry's foreign earnings, such that their company's or industry's foreign income will instead benefit significantly from the new dividend exemption/territorial system, including the GILTI tax.

Respondents' expectations of GILTI provisions' impact over the next five years (of respondents who will be impacted



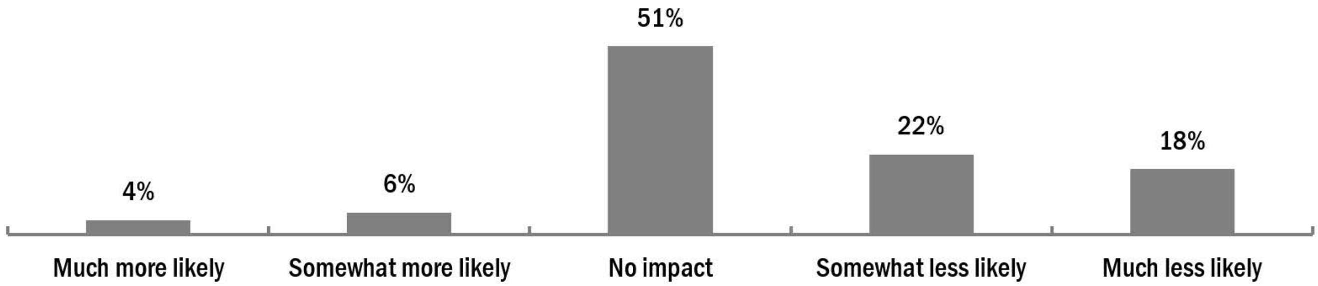
Note: Percentages may not sum to 100% due to rounding.

TCJA continues to have little impact on businesses moving production and jobs outside of the U.S.

Although some have suggested that the TCJA would help bring back jobs to the U.S. from abroad, respondents indicate that the new tax law has not affected the likelihood their company or industry will move produc-tion out of the U.S.

Of those respondents who report receiving tax benefits from the international tax provisions and/or being affected by GILTI, 51 percent say the TCJA has no impact on the location of production, while 22 percent believe it has made it somewhat less likely they will relocate production abroad. Eighteen percent of respondents believe the tax law has greatly decreased the likelihood that production will be relocated abroad, while 10 percent believe it has made it much or some-what more likely.

Likelihood of moving production and jobs outside of the U.S. after TCJA enactment



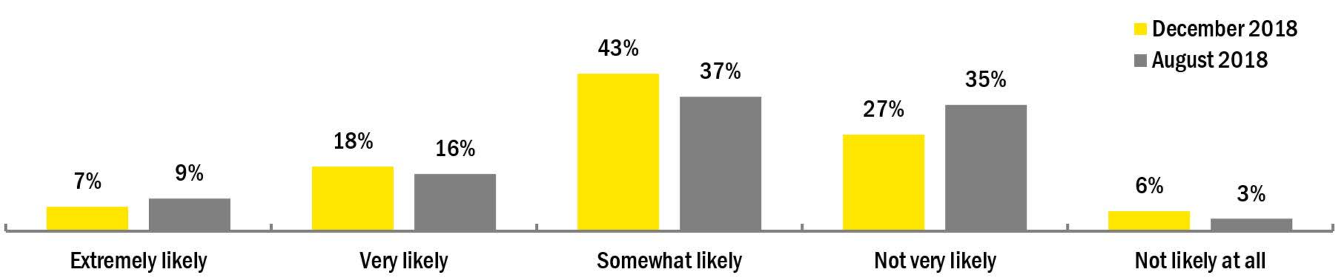
Note: Percentages may not sum to 100% due to rounding.

VIEWS ON TARIFFS AND THE ESCALATING TRADE WAR

In January 2018, the administration announced the implementation of a first round of tariffs on solar panels imported from China. In March, the administration imposed broadly applicable steel and aluminum tariffs. In April, China retaliated with its own tariffs, sparking fears of a trade war. The trade war was ''put on hold'' in May, only to be revived again almost immediately. Recent developments include additional proposed and enacted tariffs on Chinese imports, the possibility of new tariffs on imports of automobiles and automobile parts into the U.S., retaliation by major U.S. trading partners, and a new trade deal replacing NAFTA. (For updates on the U.S. trade situation, see EY's Tax Alerts, including the ''QUEST Trade Policy Brief'' and ''This Week in Trade''.)

Sixty-eight percent of respondents believe that it is at least somewhat likely that a trade war will eventually push the U.S. economy into a recession, as compared to 62 percent who responded that way in the August 2018 Barometer. Only 32 percent believe it is not very likely or not likely at all.

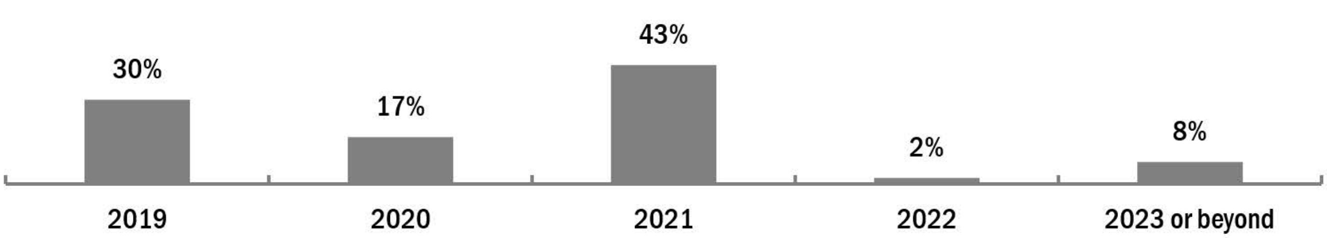
Likelihood a trade war pushes the U.S. economy into a recession



Note: Percentages may not sum to 100% due to rounding.

A majority of respondents (53 percent) believe that current trade frictions and rising tariffs between the U.S. and its major trading partners will not begin to de-escalate until 2021 or later.

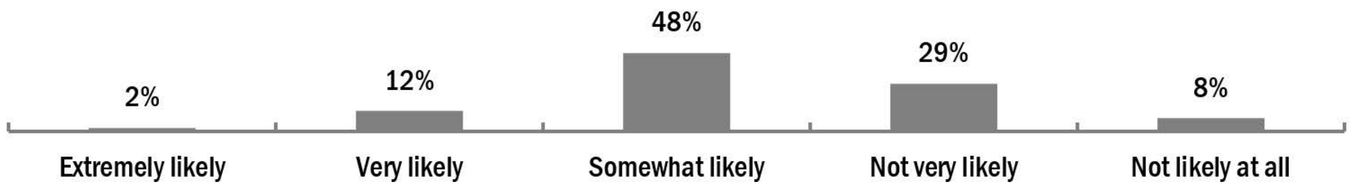
When trade frictions are expected to begin to de-escalate



Note: Percentages may not sum to 100% due to rounding.

Sixty-three percent of respondents think that it is at least somewhat likely that the administration's approach to trade policy and tariffs will succeed in getting China to reform its trade practices relating to intellectual property and forced technology transfers. However, only 12 percent and 2 percent, respectively, believe the administration's approach is very likely or extremely likely to succeed. Thirty-seven percent view the current approach as either not very likely or not likely at all to succeed.

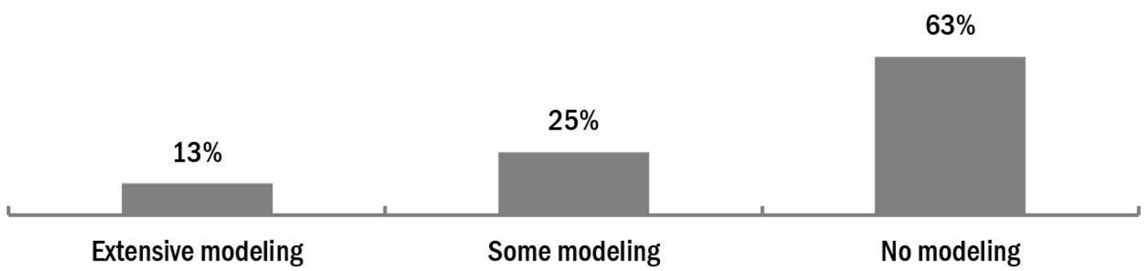
Likelihood Trump administration's approach will succeed in getting China to reform its trade practices



Note: Percentages may not sum to 100% due to rounding.

Sixty-three percent of respondents report having done no modeling of the impact of tariffs, while 38 percent report doing some or extensive modeling of the impact of tariffs on their organization, industry or markets.

Prevalence of tariff impact modeling



Note: Percentages may not sum to 100% due to rounding.

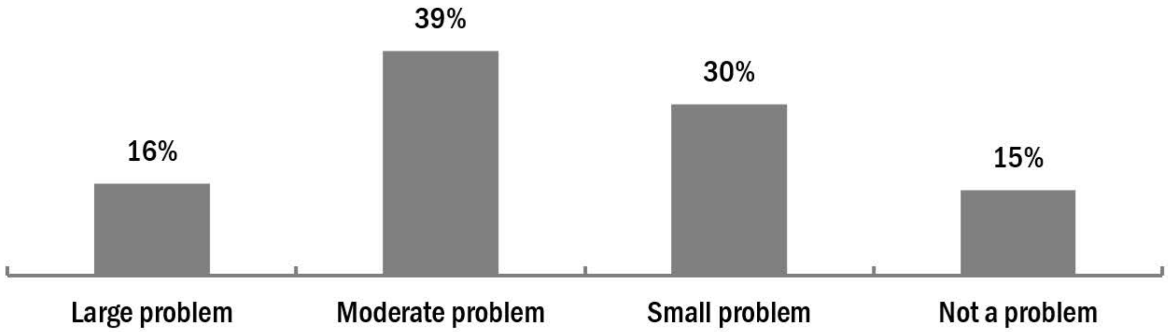
ADDRESSING INFRASTRUCTURE NEEDS AND POTENTIAL FUNDING SOURCES

In February 2018, shortly after the passage of the TCJA, the administration released an infrastructure plan estimated to cost $1.5 trillion, funded by a mix of public and private resources. Since then, there has been little update on plans to improve infrastructure, but re-sponses to the December 2018 Barometer show that in-frastructure and its funding remain a concern for most business tax professionals, companies and industries.

Deteriorating national infrastructure poses a problem for most respondents

Eighty-five percent of respondents report that deteriorating infrastructure poses at least somewhat of a problem for their business or industry, with most (39 percent) believing it represents a moderate problem. Sixteen percent believe the nation's deteriorating infrastructure presents a large problem and 30 percent say it presents a small problem. Only 15 percent report that deteriorating infrastructure is not a problem at all for their business or industry.

Magnitude of deteriorating infrastructure concerns for business or industry

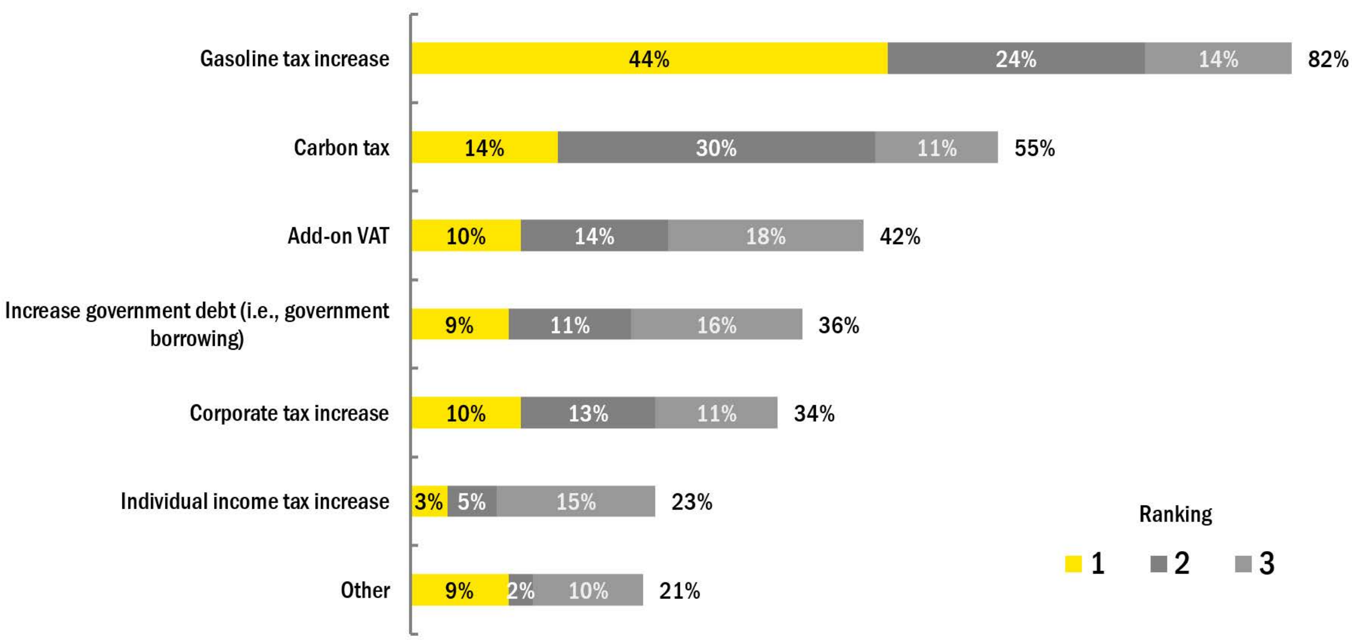


Note: Percentages may not sum to 100% due to rounding.

A higher gas tax is the preferred infrastructure financing option

Respondents overwhelmingly prefer funding U.S. government spending on infrastructure, with an increase in the gasoline tax. Eighty-two percent of respondents rank the gasoline tax as a top-three choice and 44 percent rank it as their top choice. A carbon tax is the second most popular choice, with 55 percent of respondents ranking it as one of their top three choices, followed by an add-on value-added tax (VAT) (42 percent), government borrowing (36 percent), corporate tax increase (34 percent), and individual income tax increase (23 percent). Other options respondents suggested include public-private partnerships, infrastructure-focused taxes or fees, and roadway tolls.

Top three preferred approaches to financing government spending on infrastructure



FISCAL OUTLOOK FOR THE FEDERAL GOVERNMENT

With decreased revenue projected due to the TCJA and increased federal spending, the federal deficit and debt are growing at a rapid pace, with the deficit projected to exceed $1 trillion by 2020. This December 2018 Barometer probed views regarding possible approaches to addressing the federal government's long-term fiscal imbalance.

Respondents continue to believe that major legislation to address the federal government's long-term fiscal imbalance will not be enacted anytime soon. On average, respondents believe there is a 54 percent likelihood that no legislation addressing the fiscal imbalance will be passed in the next five years. Very few respondents believe there is a high possibility of enactment in 2019 or 2020. Respondents suggest that in 2021, 2022, and 2023, the potential first three years of a new administration, there is a slightly greater likelihood of legislation being enacted.

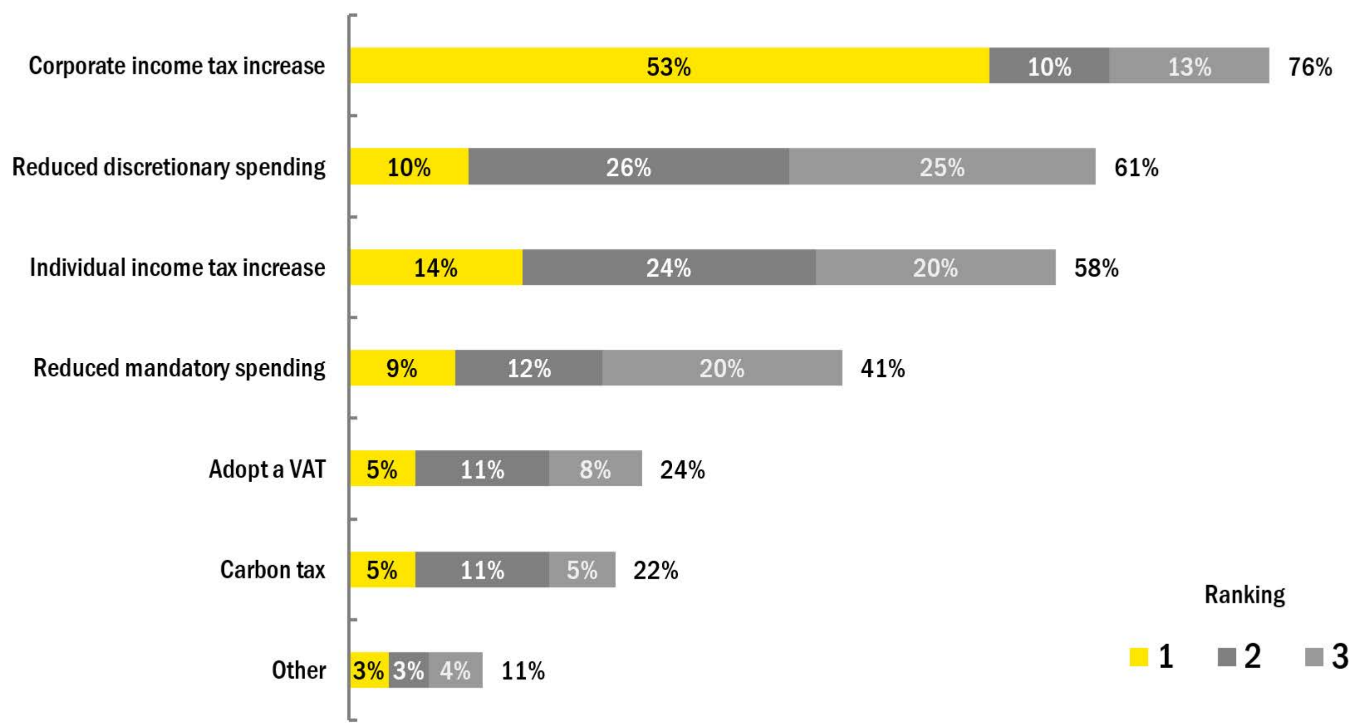
When business tax professionals expect possible legislation to address the government's long-term fis-cal imbalance

	2018	2019	2020	2021	2022	2023	No significant legislation in the next five years
December Barometer	–	4%	7%	12%	12%	11%	54%
August Barometer	2%	6%	8%	15%	11%	–	58%

Note: December and August 2018 Barometers. Per-centages may not sum to 100 percent due to rounding.

When asked about the likely approaches to significantly reducing the long-term fiscal imbalance, respondents pointed to an increase in the corporate income tax rate as the likely legislative solution. Fifty-three per-cent of respondents ranked increasing the corporate income tax rate as the most likely approach. Fourteen percent of respondents ranked an individual income tax increase as their top approach. Only 24 percent and 22 percent of respondents, respectively, included adopting a VAT or carbon tax among their three top choices.

Top three most likely approaches to reducing the long-term fiscal imbalance



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About The Tax Council and Ernst & Young LLP

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