December 13, 2017

The Honorable Kevin Brady
Chairman
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Orrin G. Hatch
Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

The Honorable Richard E. Neal
Ranking Member
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Ron Wyden
Ranking Member
Committee on Finance
United States Senate
Washington, D.C. 20510

Re: H.R. 1, the Tax Cuts and Jobs Act--Support for Applying Pass-Through Tax Reductions to Professional Service Businesses on a Non-Discriminatory Basis

Dear Chairmen Brady and Hatch and Ranking Members Neal and Wyden:

On behalf of the American Bar Association, which represents over 410,000 members, I write to express our views regarding key provisions in H.R. 1, the Tax Cuts and Jobs Act, that would bring substantial tax relief to pass-through businesses. In particular, as the conference committee works to reconcile the House and Senate-passed versions of H.R. 1, we urge you to include in the final legislation the deduction for qualified business income contained in Section 11011 of the Senate bill. We also encourage you to apply the deduction to all pass-through entities—including law firms and all other types of professional service businesses—on an equal, non-discriminatory basis.

Both the House and Senate bills include significant tax reductions for various “pass-through” businesses, including partnerships, Subchapter S corporations, and sole proprietorships. However, the pass-through provisions in the two bills differ significantly.

Under the House bill, many pass-through businesses would be taxed at a maximum rate of 25 percent on qualified business income, but any portion of the taxpayer’s net business income not deemed to be qualified business income would be treated as compensation subject to the taxpayer’s ordinary individual income tax rates. In addition, a reduced 9 percent pass-through rate would be phased in over five years for small pass-through entities based on certain income thresholds. However, the pass-through rate reduction in the House bill would generally not apply to law firms and many other types of professional service businesses.

The Senate bill would reduce taxes on pass-through businesses by creating a 23 percent deduction for the non-wage portion of the pass-through income. Unlike the House bill, the Senate measure would provide the deduction to all types of pass-through businesses, including professional service
businesses, but professional service providers could only claim the deduction if their taxable income does not exceed $500,000 for married individuals filing jointly or $250,000 for other individuals.

The ABA urges the conferees to adopt the Senate’s approach on this issue by allowing all pass-through entities—including professional service businesses—to receive a 23 percent deduction for their qualified business income on an equal basis regardless of their lines of business. We believe that this approach is far preferable to the House approach, which unfairly excludes professional service providers from the lower tax rates applicable to other non-service pass-through entities.

In our view, the pass-through provisions in the Senate bill are fairer and will promote greater economic growth than the House provisions. Law firms, accounting firms, and many other types of professional service providers create a large number of good paying jobs. In addition to directly employing many professionals and support staff, professional service providers also help stimulate job creation in the local community and throughout the nation by purchasing goods and services from numerous other businesses. Because professional service businesses provide just as many benefits to our economy and to society-at-large as other pass-through businesses, the conferees should adopt the Senate’s language—and thus create a more level playing field—by applying the same basic tax rates, deductions, and other tax benefits to all types of pass-through business entities.

Although we encourage the conferees to adopt the Senate’s approach for reducing the tax burden on our nation’s pass-through businesses, we believe that the language could be further improved by removing the arbitrary limitation that phases out the deduction for individual professional service providers earning over $250,000 (or $500,000 for married taxpayers filing jointly) but does not apply similar limits to other pass-through businesses. The ABA believes that all pass-through businesses should be treated equally, irrespective of their lines of business. Therefore, we urge the conferees to remove this arbitrary income limitation and apply the same 23 percent deduction to professional service businesses and to all other pass-through entities on a non-discriminatory basis.

Finally, while the ABA prefers the Senate’s approach to this issue, if the conference committee decides to adopt the House approach or an alternative approach, we urge it to apply the same tax benefits to all pass-through entities, including professional service businesses, on an equal basis.

Thank you for considering our views on this important issue.

Sincerely,

Hilarie Bass
President, American Bar Association

cc: Members of the Conference Committee
    The Honorable Paul D. Ryan, Speaker of the House
    The Honorable Mitch McConnell, Senate Majority Leader
    The Honorable Nancy Pelosi, House Minority Leader
    The Honorable Charles E. Schumer, Senate Minority Leader
    The Honorable David Kautter, Assistant Secretary of the Treasury (Tax Policy)