Morgan Stanley Government Relations

Washington 2017 – The First Year Preview

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With the Republican controlled 115th Congress officially sworn-in, and Donald J. Trump poised to be inaugurated as the 45th President of the United States on January 20, 2017, Morgan Stanley Government Relations summarizes the major priorities that the new Administration and Congress are set to tackle in the coming months.

Nothing will be "business as usual" in Washington in 2017, and the incoming Administration will look to govern the country in a dramatically different manner and ideological perspective than the outgoing Obama Administration. The process by which he selected his cabinet, his extensive use of social media, his continued public engagement via campaign style rallies in the post-election period, and the early controversies surrounding China, Russia and business conflicts of interest, demonstrate that President-elect Trump is prepared to take on challenges and lead the country in his own unique and unconventional way.

In the new Congress, the Republicans, as they have over the last six years, have firm control of the House of Representatives. Given its sizable majority, the Republican House leadership will be able to move almost any measure through the chamber with the most likely serious resistance, if any, coming from potential policy differences between the conservative fiscal hawk deficit and debt conscious wing of the GOP and the "Trumpist" Republican wing that is prepared to support the ambitious (and expensive) spending proposals of the Trump Administration.

Another very real impediment to the GOP and Trump legislative agenda is the narrower margin of Republican control in the Senate. With the Senate comprised of 52 Republicans and 48 Democrats, for most controversial legislative initiatives, the Republican leadership will need to craft legislation in a way that will entice eight Democratic Senators to cross party lines to support the Republican proposal. With 10 of the 25 Senate Democrats facing reelection in 2018 coming from states that Donald Trump won in November 2016, the Senate Republican path forward will be to regularly target these reelection vulnerable Senate Democrats.

The Top Legislative Priorities in 2017

Repeal of Affordable Care Act (Obamacare) – President-elect Trump and the Republican Congressional leadership have stated that the repeal of the Affordable Care Act (ACA) is their top priority and will seek to have the repeal bill on the new President's desk in the first days of his Administration. The new Congress, in early January, is expected to adopt its 2017 Budget Resolution, and as a part of this budget initiative, direct Congress to repeal ACA and its associated tax provisions (e.g., the 3.8% Medicare tax on investment income and the 0.9% Medicare Part A tax increase) and individual/employer mandates. By a simple majority in the House and Senate, the Congress is expected to quickly repeal the ACA. The Congress, however, will not effectively repeal the ACA *immediately*, but most likely establish an interim transition period that gives the Congress anywhere from two to three years (to be determined) to develop a replacement health care program to fill the void of repeal. Many Congressional Republicans are calling for an extended transitional period that will allow the Republicans to develop a bipartisan plan that can be subsequently adopted to address the needs of the 20 million Americans that have relied on the ACA. The Republican replacement plan is certain to be highly controversial and given the breadth of diverse health care interests and constituencies, its ultimate success is uncertain.

Comprehensive Tax Reform – President-elect Trump, Speaker of the House Paul Ryan, and Senate Finance Committee Chairman Orrin Hatch are prepared to move comprehensive tax reform through the House and Senate in 2017. Most likely using the FY 2018 Budget Resolution as its vehicle to secure success with a simple majority, all expectations are that federal tax reform will be accomplished by August or fall 2017. In the early months of 2017, the congressional tax committees and the new Administration will negotiate a broad based tax measure that will almost certainly lower corporate tax rates to the 20% range, establish a process and new rate for repatriating previously untaxed offshore earnings back to the U.S., look to implement a territorial tax system, adjust depreciation schedules, lower the small business pass-through tax rates, reduce and simplify individual tax rates, and most controversially, adjust, reduce and modify the broad array of business and individual tax deductions that many are accustomed to taking. The development and passage of U.S. tax reform is the ultimate legislative “horse trade” exercise – a process of intense negotiation, deal making, fine tuning and numerical adjustments. Although the tax reform measure is initially expected to cost the U.S. Treasury approximately $2 trillion to $4 trillion, depending on corresponding offsets or “revenue raisers” (e.g., the elimination or haircut of deductions allowed or tax revenue raising adjustments) and the estimated U.S. economic growth prospects resulting from lower taxes, it is the tax writers’ goal to enact tax reform that is “deficit neutral” − a move that would also appease the Republican fiscal hawks concerned with runaway U.S. federal deficits and debt loads.

Although the finer details will remain uncertain until the end, the political momentum and impetus to get tax reform done could not be clearer, and we have a difficult time seeing how business and individual tax reform will not be in place for Americans in 2018. In the coming month, as the process unfolds, Morgan Stanley Government Relations will be providing a closer look at the development of comprehensive federal tax reform and more specifically, what we can expect.

U.S. Infrastructure Investment – Candidate Trump, as well as President-elect Trump, made ambitious infrastructure spending and investment a major domestic priority upon taking office. On the campaign trail, President-elect Trump promised $500 billion in U.S. infrastructure investment, and subsequently, increased his spending goal to $1 trillion. Federal stimulus spending at this level has not been publically supported by many Republican fiscal hawks (in years past or of late), and most recently, Speaker Ryan and Senate Republican Leader McConnell have said that they are not interested in pursuing public spending at these levels and remain focused on ACA repeal and tax reform in 2017. The Administration and Congress will explore the public spending options, public-private partnerships, private sector investment incentives, tax-exempt bond programs, the creation of an infrastructure bank, and other means to advance infrastructure spending. However, we expect the ambitious infrastructure spending initiative to be delayed in 2017 as the Congress looks to tackle and complete tax reform.

Financial Services Reform – President-elect Trump and the Republican congressional leadership have promised a full reexamination of the Dodd-Frank Act (DFA) and the many regulations that have negatively impacted lending and job creation, and unnecessarily overburdened small and medium sized financial institutions. House Financial Services Chairman Hensarling is preparing to modify and reintroduce his broad sweeping financial reform bill (“The Financial CHOICE Act”) that provides small and medium sized banks relief from the regulatory burdens and obligations of DFA, repeals the Department of Labor’s Fiduciary Duty Rule and prohibits the DOL from promulgating any similar rule until the SEC first exercises its authority on the topic, modifies the operations of the Financial Services Oversight Council and the Consumer Financial Protection Board, increases oversight and accountability of the Federal Reserve, and provides sweeping DFA regulatory relief to large financial institutions that meet a new higher leverage ratio. It is our expectation that Chairman Hensarling will successfully move his Financial Choice Act through his committee and the House of Representatives this spring.

The more methodical action will occur in the Senate, where new Senate Banking Committee Chairman Crapo will need to find middle ground with at least eight Senate Democrats to move compromise financial services reform. We expect Chairman Crapo and moderate Senate Democrats to find agreement around providing relief for smaller financial institutions, but the real challenge will be adding provisions intended to roll back other provisions of DFA that will be strongly opposed by Senators Elizabeth Warren and Bernie Sanders as well as most liberal Democrats.

Given the dynamic in the Senate, we expect financial services reform legislation to move slowly through 2017 with any final compromise agreement not occurring until late in the year or some point in the first half of 2018.

With respect to the Department of Labor's Fiduciary Rule, we expect the incoming DOL to embark in a review of the impact of the rule, as well as potentially delay the rule's implementation for a period of time. The DOL will use any period of delayed implementation to revisit the rule, its impact on investors, and potentially seek to modify the rule as it sees appropriate. Separate from the effort in the CHOICE Act, the Republican led Congress will also look to revisit the DOL rule early in 2017, with the key House and Senate Labor Committees potentially taking legislative action to modify or roll back the rule. Senate action on any DOL related legislation will also face strong Democratic opposition and the 60-vote obstacle will almost certainly slow down any quick legislative fix.

Sweeping Regulatory Reform – As President-elect Trump spent much of November and December selecting the members of his cabinet, it became clear that he will install a government that will spend the next four years modifying and reversing the regulatory policies of the Obama Administration. From energy (refocus on coal and oil, as well as energy exportation) to the environment (review of the Clean Air Act and Clean Water Act regulations and EPA mandates) to labor (minimum wage rules, workplace regulations, the DOL fiduciary duty rule) to telecommunications (internet neutrality rules) to financial services (broad review of DFA regulations and bank regulatory, SEC and CFTC rules) to antitrust regulation, the new Administration will undertake a full and sweeping review of regulations that it believes have proven excessive, unjustified, overly burdensome and impeding economic growth and job creation. This effort will be extensive and will take time to evolve, but the regulatory environment at the end of 2020 will be very different than the regulatory environment of 2016.

The Known Unknowns and Foreseeable Challenges – Every Administration is tested early on and faces domestic and international challenges that can distract from successfully accomplishing their expressed agendas. It appears that recent interactions with China and the many questions surrounding Russia's meddling in the U.S. election will test the new Administration and Congress in the early weeks and months of the new term. How Iran reacts to the President-elect's pronouncement to withdraw from the multi-country nuclear arms deal could also have the potential to disrupt and distract. Domestically, an emotional and divisive battle over a Supreme Court nominee in the first 100 days will almost certainly consume the Congress, the media and the country. These are a few of the major "known unknowns" – and of course it is the unknown and impossible to predict events that truly test one's leadership, ability to handle crisis, and skills to soundly and confidently govern.

Morgan Stanley Government Relations will continue throughout the year to provide insight and analysis on the Trump Administration and Congressional agendas, their execution and their impact on Morgan Stanley and our clients.

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