A Foundation for Tax Reform? The Trump Administration's Tax Proposals

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*The information in this article is current as of its submission on February 6, 2017. Any changes or updates in legislation or executive acts since that date are not reflected.

Introduction

Throughout his campaign, President Donald Trump endorsed an aggressive set of tax proposals that, if enacted, would impact nearly every taxpayer in the United States. Under these proposals, both individuals and businesses would reap the rewards of many potential favorable changes, while others would face increased taxes. The proposals have been adjusted from time to time throughout the campaign and the beginning of the President's term. The following explores the various tax proposals and early actions of President Trump, which could provide a sneak-peak into the framework of the most comprehensive federal tax reform in more than 30 years.

Trump's Tax Plan

President Trump's tax plan ("Plan") sets out four goals: (1) tax relief for middle-class Americans; (2) simplifying the Internal Revenue Code; (3) growing the American economy; and (4) not adding to the national debt or deficit. The Plan seeks to meet these goals by eliminating the estate tax and the alternative minimum tax (AMT), capping corporate income tax rates at 15 percent and reducing the number of individual income tax brackets. The details of the Plan are discussed below.

Individual Income Taxes

The Plan reduces the number of tax brackets from seven to four. The Plan would also eliminate the marriage penalty, as well as the Head of Household filing status. The new rate schedule would be:

Income Tax Rates	Long Term Capital Gains / Dividends Rates	Single Filers	Married
12 percent	0 percent	$0 to $37,499	$0 to $74,999
25 percent	15 percent	$37,500 to $112,499	$75,000 to $224,999
33 percent	20 percent	$112,500+	$225,000+

The new tax brackets would mean a reduction in income taxes for most individuals. However, there is a select group of middle-income earners that would pay more in individual income taxes under the Plan than they pay under current law. Specifically, those taxpayers currently in the upper half of the 28 percent brackets would be in the 33 percent bracket under the Plan. Additionally, taxpayers in the 10 percent bracket would be placed in the 12 percent bracket. The existing rate structure for capital gains (currently a maximum of 20 percent) would be retained, but carried interests would be taxed at the higher ordinary income rates.

The Plan will also increase the standard deductions for single filers to $15,000 ($30,000 for married filing jointly). While the Trump Administration has indicated that this should eliminate the need for many itemized deductions, there has been little information provided regarding changes to most deductions. The Administration has indicated that the mortgage interest deduction will remain intact. Itemized deductions in general, however, would be capped at $100,000 for single filers ($200,000 for married filing jointly).

In addition, the Plan allows an above-the-line deduction for expenses for childcare and dependent eldercare. There would also be childcare spending rebates via the Earned Income Tax Credit for certain low-income taxpayers. All taxpayers would also be permitted to establish a dependent care savings account (DCSA), funded with up to $2,000 per year. The government would provide a 50 percent match of up to $1,000 to a DCSA for low-income families. The unused balance would roll over each year.

In connection with the President's proposed repeal of the Affordable Care Act (ACA), several revenue-raising taxes created by the ACA could be eliminated. These include the 3.8 percent tax on net investment income and the additional 0.9 percent Medicare payroll tax on high income earners, plus the excise tax on manufacturers of medical devices. Full repeal of the ACA would also reduce the threshold for itemized deductions for out-of-pocket medical expenses back down to 7.5 percent (from 10 percent currently) of adjusted gross income.

Estate Tax

The Plan proposes a complete elimination of the federal estate tax. Currently, this tax only impacts estates with assets in excess of $5.49 million (nearly $11 million for married couples). This affects approximately 5,000 estates each year. The Plan would also disallow contributions of appreciated assets into private foundations established by the decedent or the decedent's relatives.

Corporate Taxes

The centerpiece of the Plan is the cut in the top corporate tax rate from 35 percent down to 15 percent. The Plan also eliminates the corporate AMT. The rate applies to all businesses in the United States that retain all profits within the country. Most corporate tax credits would be eliminated, with the exception of the research and development credit.

The Plan also provides a "deemed" repatriation of corporate profits currently held offshore. A one-time 10 percent tax would be imposed on all of a U.S. corporation's overseas profits in order to incentivize corporations to return these for investment in the United States.

The Plan also provides for additional tax credits for businesses providing childcare assistance. The cap for on-site childcare credit would increase from $150,000 to $500,000 per year and the recapture period for this credit would be reduced from 10 years to 5 years.

It is important to keep in mind that the Plan is nothing more than a proposal at this time. To take effect, Congress would need to enact legislation. As of now, the proposed tax plan from the Republicans in Congress varies from the President's Plan in several significant ways. It is likely that in reaching common ground, some of the Plan's proposals will need to be dropped, while others would require modifications. The plans are both built on the premise that it is necessary to simplify the tax code, but differ in the best way to accomplish this goal. There is also substantial disagreement among scholars and politicians as to whether changing the tax brackets will have any real impact on simplifying the tax code. Critics of the Plan argue it is more important to focus on the earned income credit, education credits, and other, more complex, aspects of the Internal Revenue Code. The plans also both seek to reduce taxes for the middle class, but again approach the issue with varying methods.

Although not formally part of the Plan, the President has also publicly reaffirmed his desire to repeal the so called "Johnson Amendment" applicable to section 501(c)(3) organizations. Such a repeal would permit section 501(c)(3) public charities, including churches and other religious organizations, to freely engage in political activities and endorse candidates for public office without jeopardizing their tax-exempt status.

White House Memoranda and Executive Orders

Several of the President's initial actions following his inauguration have the potential to affect tax law on a different front. For example, on his first day in office, the President's chief of staff issued a "Memorandum for the Heads of Executive Departments and Agencies" calling for a freeze on the further issuance of regulations across all governmental agencies. Any regulation not printed by the Office of the Federal Register (OFR) by noon on January 20, 2017 was directed to be held by the issuing agency until reviewed by a department or agency head appointed by the President. Any regulations already submitted to OFR were to be immediately withdrawn. Further, any regulations already published but not yet in effect were to be postponed. These regulations must have an effective date of 60 days after January 20, 2017 to allow the appointed department or agency head an opportunity to review.

Most tax laws enacted by Congress have accompanying regulations providing details necessary to interpret the laws and sometimes regulations are required to implement the laws. This apparently broad regulatory freeze has the potential to adversely affect a number of IRS regulatory projects already in process, including those that are expected to provide taxpayer-favorable rules.

While the regulatory freeze is likely to have a major impact on all federal agencies, there are several sets of significant tax-related Treasury regulations currently in limbo as a result of the freeze. The long-anticipated proposed regulations addressing the new centralized partnership audit procedures appeared online on January 18, 2017 and were scheduled to be printed by the OFR on January 25, 2017, but due to the January 20 memorandum, the proposed rules were withdrawn prior to printing. These proposed regulations are immense and important to the handling of partnership audits beginning with the 2018 tax year. If regulations are not put in place, the law will be difficult, if not impossible, to implement. Thus, it is worthwhile for those who will be advising clients with regard to partnership audit issues to stay apprised of the developments in this area when the proposed regulations are eventually released. It is unclear what, if any, changes will be incorporated into the proposed rules from their previously distributed (and withdrawn) form.

On January 30, 2017, President Trump issued a separate Executive Order (EO) to reduce regulations and control regulatory costs. The common phrase associated with this EO is "2 for 1," as described by White House spokespeople. At its core, the 2-for-1 EO essentially provides that for any one new regulation issued by an executive agency, two existing regulations must be repealed. This EO follows a campaign promise to reduce regulation across the government.

In addition to calling for the repeal of two current regulations to issue one new regulation, this EO mandates that for the current fiscal year, the total cost of all new regulations may not exceed $0. To accommodate this static budget, the cost of any new regulation must be offset by the costs saved from repealing other regulations. This cost elimination must comply with the Administrative Procedure Act and other applicable law. Additional guidance is supposed to be issued to address compliance with this section of the EO.

This limit on new regulations will carry forward to the 2018 fiscal year. Any proposed regulations for 2018 will need to be included in the Unified Regulatory Agenda. No other new regulations will be permitted unless approved in advance in writing by the Director of the Office of Management and Budget (OMB).

While this regulatory trim will impact all agencies, a February 2, 2017 memorandum issued by the Acting Administrator of the Office of Information and Regulatory Affairs (OIRA) indicates that the IRS may be immune from most of the impact of the 2-for-1 EO. In the form of questions and answers, this "Interim Guidance Memorandum" provides that the 2-for-1 EO will only apply to "significant" regulatory actions.

The Government Accountability Office (GAO) has previously determined that most IRS regulations are not deemed "significant" by the OIRA. *See* GAO-16-720. The IRS and Treasury officials generally view any economic impact of a regulation as stemming from the underlying statute, and thus, rarely designate tax regulations as "economically significant." Accordingly, for now it appears that most IRS regulations will be exempt from the 2-for-1 EO.

Conclusion

The President's Plan proposes several significant changes to the current tax regime, particularly with respect to tax rates and corporations. Whether these changes become part of a broader tax reform package from Congress remains to be seen. More immediate, the freeze on the release of new regulations has had and will have an immediate impact on the notice and comment rulemaking process, and, depending the amount of time it takes for proposed rules to be reviewed internally, could impact the IRS's, and other agencies', abilities to function. While the 2-for-1 EO is apparently not applicable to most IRS regulations, if the EO is revised or reissued to include (or is later interpreted to include) these regulations, there could be a substantial impact on the ability of the IRS to continue its numerous regulatory projects and possibly hamper the issuance other types of non-regulatory guidance (*e.g.*, Revenue Rulings). Practitioners in tax and other regulated areas of the law are encouraged to stay advised of updates.

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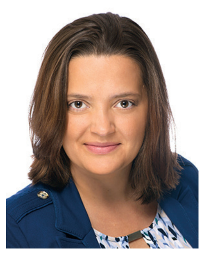

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William G. Schneider Jr.

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Bill has requested that any gifts in his honor be made to the Louisville Bar Foundation's endowment fund.

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2017 Summer Law Institute Applications Available

Applications are now being accepted for the LBA's annual Summer Law Institute, a law camp for high school students interested in the law or legal careers. The 2017 camp, scheduled for June 11 – 17, is a partnership between the LBA, Brandeis School of Law and Bellarmine University.

The application deadline is April 11 and application packets are available on the LBA website or by contacting Lisa Hebert, *lhebert@loubar.org*. Tuition is $175 and a limited number of scholarships are available. SLI is funded in part through the Louisville Bar Foundation. ■

It May be Gray Outside, but it's Time to Plan for Summer Interns

Summer will be here soon and the LBA is in the process of finding full and part time jobs for Central High School Law & Government students. Why not take a chance on a high school student? The impact on both the student and your firm just might have a lasting effect on our legal community.

The Summer Intern Program is a partnership between the LBA and Central High School that allows students the opportunity to intern for local law firms and offices, gaining insight into the legal profession and the opportunity to interact with legal professionals, as well as valuable work experience. In turn, the SIP affords employers increased productivity, the opportunity to impact the future of the profession, and a great diversity initiative. Demetrius Holloway of Stites & Harbison said the firm was "blessed by their presence and inspired by their desire to succeed."

These jobs have been life changing for many of these students. And the cost is as little as $1,500 for part-time and $3,000 for a full time student. If you can't hire directly, your firm can also sponsor a student to work at Legal Aid or the Public Defender's Office.

Please contact Lisa Hebert at 583-5314 or at *lhebert@loubar.org* if you can help a student this summer. ■