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Trump Administration Tax Proposal – September 27, 2017

The Trump Administration today released its much awaited tax reform proposal the highlights of which are set forth below. The proposal, which has been developed in collaboration with the House Committee on Ways and Means and the Senate Committee on Finance was issued in the form of a "unified framework", entitled "Unified Framework For Fixing Our Broken Tax Code". The framework provides a clear outline of the administration's aspirational objectives but leaves out detailed guidance. The framework states that it is intended to serve as a template for the tax writing committees that will develop legislation through a transparent and inclusive committee process, and that the administration welcomes bipartisan support and participation in the process.

Standard Deduction

The standard deduction for individuals would be increased to $24,000 for married taxpayers filing jointly and $12,000 for single taxpayers.

Individual Tax Rate Structure

Individual tax brackets would be consolidated into three brackets of 12%, 25% and 35%. The framework leaves open the possibility to add another tax bracket for the highest-income taxpayers.

Child Tax Credit

The proposal repeals the personal exemption for dependents and increases the child tax credit.

Individual Alternative Minimum Tax

The proposal repeals the individual alternative minimum tax.

Itemized deductions

The framework repeals "most" itemized deductions but retains the deductions for mortgage interest and charitable contributions. The framework is silent as to the deductions for state and local taxes but it appears that those are among the eliminated itemized deductions.

Retirement

The proposal does not contain any details but appears to retain tax incentives for individual contributions to retirement plans.

Estate and Generation-Skipping Transfer Taxes

The estate and generation-skipping transfer taxes would be repealed.

Tax Rate Structure for Corporations

The framework reduces the corporate tax rate to 20%.

Corporate Alternative Minimum Tax

The framework eliminates the corporate alternative minimum tax.

Expensing of Capital Investments

The framework would allow immediate expensing of investments in depreciable assets for 5 years. The proposal would exclude however the expensing of "structures" made after September 27, 2017. The framework does not elaborate on the scope and purpose of this limitation.

Interest Expense

The interest expense deductions for C corporations will be "partially" limited. The scope of this limitation is unclear. In addition, the committees will consider the deductibility of interest by non-corporate taxpayers.

Bonus Depreciation and Tax Credits

The proposal eliminates bonus depreciation and envisions the elimination of all business credits except (1) R&D credits and (2) low-income housing credits. The framework states that while it contemplates the repeal of all other credits the committees may decide to retain certain credits budgetary limitations allowing.

Tax Rules Affecting Specific Industries

The framework contains no details in this regard but indicates that it intends to modernize special tax regimes affecting certain industries and sectors.

Tax Rate Structure for Pass-throughs/Small Businesses

The framework limits the maximum tax rate applied to business profits of small and family owned pass-throughs to 25% as opposed to the top individual rate. Small business pass-through entities would include sole proprietorships, partnerships, and S corporations. The framework leaves it to the committees to define business profits in order to ensure that compensation to partners for services is taxed at the individual rates and not at the lower pass-through rates.

The framework is silent as to the tax treatment of carried interests.

International Aspects

As expected the framework does not contain any “border adjustment tax” proposal. However, the framework does contain proposals that would fundamentally affect the taxation of offshore earnings of U.S. companies. In addition, the framework does provide for the repatriation of offshore earnings currently held by U.S. multinationals in foreign subsidiaries.

The framework aims to eliminate the tax incentive to multinationals to keep foreign earnings offshore by fully exempting dividends repatriated by foreign subsidiaries in which a U.S. parent company owns at least a 10% stake. As a transitional step, the framework would effectively treat existing offshore earnings as having been deemed repatriated. Although lacking in detail, the framework would tax such deemed repatriation presumably at a favorable tax rate (not included in the framework), and spread out payment of the tax liability over a period of several years (also not defined in the framework). The framework does specify that offshore earnings invested in illiquid assets would be taxed at a lower rate than those held in cash and cash equivalents.

Taking aim at the offshoring of capital and jobs, the framework seeks to prevent offshore shifting of profits by taxing at reduced rates and on a global basis the foreign profits of U.S. multinational corporations. The framework states that committees will develop rules to address taxation of U.S. headquartered parent companies and foreign-headquartered parent companies so as level the playing field between the two structures. The framework provides no description of what those rules may be.

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