



## Tracking Tax Reform

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On April 26, 2017, Treasury Secretary Steven Mnuchin and White House chief economic advisor Gary Cohn announced President Trump's latest tax reform proposals, titled "2017 Tax Reform for Economic Growth and American Jobs" and described as "the biggest individual and business tax cut in American history." These proposals differ from President Trump's proposals on the campaign trail, and also differ from the House Republicans proposals in their blueprint "A Better Way." The proposals are very high-level, and Mnuchin and Cohn stressed several times that the administration is still working out the details of the plan. Our previous [Tracking Tax Reform](#) article, published on April 5, 2017, details the proposals in the House Republican blueprint and the proposals made by President Trump on the campaign trail.

### Individual Taxation.

- **Streamlining returns.** Consistent with his message on the campaign trail, President Trump reiterated his desire to simplify the tax code.
- **Rates.** President Trump proposed reducing the number of tax brackets (ranging from 10% to 39.6%) down to three brackets – 10%, 25%, and 35%. These brackets differ slightly from the brackets he proposed on the campaign trail (12%, 25%, and 33%), most notably reducing the tax cut for the highest bracket. It remains unclear what income amounts will be taxed in each bracket, with Mnuchin and Cohn stating that further details will be forthcoming, but insisting that the proposals will provide tax relief to middle-income families. President Trump called for the elimination of the 3.8% surtax on net investment income exceeding \$200,000 (\$250,000 for those married filing jointly) used to fund Obamacare, even though it is currently unclear if the Affordable Care Act will also be repealed. The 0.9% Medicare surtax on wages over \$200,000 (\$250,000 for those married filing jointly) was not addressed. President Trump also called for the repeal of the "death tax" (i.e. the estate tax), which applies an additional tax on individuals who die with an estate worth over \$5.49 million. President Trump's proposal did not mention the gift tax or the carryover basis rules (rules that in certain situations allow heirs to inherit the decedent's original tax basis in inherited property, plus the value of improvements).
- **Increase in standard deduction, elimination of almost all itemized deductions.** President Trump proposed doubling the standard deduction to \$12,700 for individuals and \$24,000 for married couples filing jointly. President Trump proposed the elimination of all tax deductions other than for mortgage interest and charitable contributions. Notably, this would eliminate the federal tax deduction for state and local income tax. Cohn noted that retirement incentives would remain intact and that the tax code would provide relief for child and dependent care, but did not elaborate as to how.
- **Elimination of the Alternative Minimum Tax.** Consistent with his message on the campaign trail, President Trump called for the complete elimination of the Alternative Minimum Tax for individuals.
- **Taxation of investment income.** Also consistent with his message on the campaign trail, President Trump has proposed maintaining the current taxation system for dividends and capital gains, leaving the top rate at 20%.

### Business Entity Taxation.

- **Rates.** President Trump proposed a flat 15% tax on corporate income, the same corporate tax rate he proposed on the campaign trail.
- **Taxation of pass-through income to entity owners.** President Trump seemed to propose taxing income derived from pass-through entities (i.e., S corporations, LLCs, partnerships) to their owners at a rate of 15%, rather than the ordinary individual income tax rates that such income is currently taxed at. When pressed regarding whether this would provide a loophole for pass-through entity owners to re-characterize wage income (taxed at the higher individual tax rates) as income derived through the pass-through entity, Mnuchin insisted that the administration will "make sure that there are rules in place so that wealthy people can't create pass-throughs and use that as a mechanism to avoid paying the tax rate they should be paying

on the personal side.” It remains unclear how such rules to prevent tax avoidance would be enforced. Mnuchin may have been referring to the House Republican blueprint proposal that seeks to apply a lower tax rate to active business income earned through a pass-through entity *after* the deemed payment of reasonable compensation to owners and partners that also provide services to the entity, as a means of preventing tax avoidance. It is not clear how such reasonable compensation would be calculated.

- **Changes to depreciation and interest deductions.** President Trump did not make any specific proposals regarding depreciation or interest deductions. President Trump has previously suggested a system of optional expensing of investments for certain manufacturers, where manufacturers that elect to immediately expense capital investments would lose the corporate interest expense.
- **Business incentives.** President Trump vaguely stated that he wants to eliminate tax breaks for special interests. This could potentially mean that all business incentives for specific industries, such as real estate and oil and gas, could be eliminated. It could also mean that President Trump wants to repeal the R&D credit, but at this time it is unclear.
- **Carried Interest.** President Trump did not make any statement or proposal regarding carried interests. President Trump has previously stated that he will tax carried interest income as ordinary income, but if his latest proposals regarding the taxation of income earned through pass-through entities were to pass, this rate could potentially be 15%.

### International Taxation.

- **Tax on future foreign earnings.** President Trump has proposed adopting a territorial tax system, which would not impose a tax on corporate income earned outside of the United States, even when that income is repatriated.
- **Tax on accumulated foreign earnings.** President Trump has proposed a one-time mandatory tax “on trillions of dollars held overseas,” but did not elaborate on what tax rate might apply to those accumulated offshore earnings, only that it would be a “competitive rate.”
- **Border Adjustment Tax.** Notably, President Trump’s latest proposals contain no mention of the controversial Border Adjustment Tax, favored by Speaker Paul Ryan.

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