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Trump Tax Plan Could Impact 2016 Year-End Planning

Donald Trump's surprise victory first rattled markets, then invigorated them. It triggered protests, and in some circles, is even fueling a "CalExit" movement for California to break away from the union. But, it could invite some tax planning, too. Candidate Trump made no secret of his view that our tax system needs reform. He even sounded briefly Warren Buffet-like. He blamed the tax laws for making it possible for him to manipulate the tax law to pay so little via his controversial $916 million net operating loss!

With Republicans retaining control over the House and Senate, some tax cuts are inevitable. With this quite extraordinary confluence of events, President-elect Trump and Congress might tell the tax code, "*you're fired!*" This could suggest that deferring income into next year if you can might be wise. Next year, the rates should be lower. Under current law, we pay tax on ordinary income tax at graduated rates stretching from 10% to 39.6%.

But since Obamacare, high-income taxpayers pay an additional 3.8% surtax on net investment income. That means the top federal rate for individuals is really 43.4%. Qualified dividends and long-term capital gains are taxed at 15% or 20%, depending on your income. Yet, that rate too gets hit with the additional 3.8% for Obamacare's net investment income tax. Here are 5 key things about the Trump tax plan:

1. Individual Rate Cuts. Trump proposes cutting the tax brackets to three: 12%, 25%, and 33%. He would eliminate Obamacare's 3.8% net investment income tax, too. As a result, the top rate would be 33%, with the top rate on capital gains and dividends a firm 20%. There are some drawbacks, though, that may alter your usual tax planning. For example, Trump's tax plans call for slashing itemized deductions. Under Trump's plan, personal exemptions are eliminated. High earners already do not deduct personal exemptions due to the phase out, so this should have little impact. More consequential, though, is that itemized deductions would be capped at $200,000 for married couples. Paying state taxes before year-end means you can deduct them now. And the same for charitable contributions.

2. Business Tax Cuts. Businesses are supposed to be in for big tax cuts. Corporations currently pay 35%. President-elect Trump would cut it to 15%. But he would eliminate most business deductions. And there would be simplicity. Instead of depreciation over many years, he would allow up-front

deductions. But forget deducting interest on debt, he has suggested. LLCs, partnerships and S corporations would have changes too. Candidate Trump suggested that the owners of these entities should pay the same 15% rate as corporations. Astoundingly, that could mean someone taxed at 39.6% or even 43.4% on flow-through business income now, could see their tax rate slashed to 15%! Of all the proposed tax changes, this one — if it happens — may be the most momentous.

Already, some people are wondering if they can cash in. For example, can wage earners who are paying high income taxes now become independent contractors by forming an entity and conducting their own business? If you pay 39.6% now and could pay 15% by doing that, the incentives are huge. Of course, there are already huge fights and audits over worker status issues. And this change (if it happens) would most likely increase them. It is hard to figure how to handle this one before year-end. Some people will

3. Overseas Profits. Another change that could impact many international companies based in the U.S. would address the billions in overseas profits. These billions are currently escaping the U.S. tax system entirely. Trump's plan would impose up to a 10% deemed repatriation tax on the accumulated profits of foreign subsidiaries of U.S. companies.

That 10% toll charge would be payable over 10 years, Trump has proposed. Trump and his team say this change would trigger a huge inflow of funds back to the U.S. And for the future, Trump's proposals would tax future profits of foreign subsidiaries of U.S. companies each year as the profits are earned. With these changes possible, companies will wait and see.

4. No Death Tax. The estate (or death) tax is another one Trump hates, though you probably just have to wait to see on this one. It still pays to have some kind of estate plan until then. And try to stay healthy! Under current law, you can pass up to $5.45 million to your heirs tax-free. That is doubled for a married couple. But beyond this, you pay an estate tax of 40%. It is entirely separate from income taxes. Hillary Clinton had proposed cutting the exemption materially from $5.45 million to $3.5 million. She also wanted to raise the estate tax rates to 50% and even 65% in some cases. The president-elect said he would repeal it entirely.

If the estate tax is repealed, step-up in basis at death will go to. Under current law, for income tax purposes, any appreciation in your assets gets a stepped-up basis to the value on your date of death. That way you don't pay *both* income and estate tax on exactly the same dollars. But if the estate tax is repealed, Trump's proposal would allow income tax on the appreciation inherent in the assets for an estate valued in excess of $10 million. However, you would only pay this income tax when the beneficiary sells the assets.

5. Top v. Bottom. Not everyone is wild about the Trump proposals. Much of the criticism of Trump's tax plans are that he would give the biggest breaks to the highest earners. Yet supporters like to invoke President Reagan. Trump and his team have suggested that loosening of capital at the top will encourage investment, trigger transactions, create jobs and fuel economic growth. Change in the tax world is constant. Yet by any standards, some of the tax changes likely in 2017 and beyond are going to be huge.

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