November 17, 2016

To Our Clients and Friends:

The past few days have certainly brought about a whirlwind of surprise. Donald Trump's election as the 45th President of the United States on November 8 is expected to bring changes to the tax laws for individuals and businesses. President-elect Trump had made tax reduction a centerpiece of his economic plans during his campaign, saying he would, among other things, propose lower and consolidated individual income tax rates, expand tax breaks for families, and repeal the Affordable Care Act. As the next few weeks and months unfold, taxpayers will learn more about Trump's tax plans.

More immediately, the results of the November 8 election may impact year-end 2016 tax planning, because of last-minute provisions soon expected to be passed by the "lame-duck" Congress-or by the new Congress early in 2017.

Further, the 115th Congress, which will convene in January 2017, will find the GOP in control of both the House and Senate, therefore allowing Trump to more easily move forward his proposals. It remains to be seen, however, what compromises will be necessary between Congress and the Trump Administration to find common ground. And beyond moving forward individual tax proposals, it also remains to be seen whether they can be packaged within a mandate for broader "tax reform" and "tax simplification."

This briefing is based on President-elect Trump's statements and proposals on taxes and tax policy during the campaign. Trump's tax-related proposals may change after he assumes office in January 2017. The House Ways and Means Committee is currently working on legislation based upon the House GOP "Better Way" tax reform blueprint that was released in June. The "Better Way" blueprint shares some similarities with proposals mentioned by Trump during his campaign. Although tax reform hearings that have been held over the past several years have laid foundation of data on which reform proposals may be considered, it is uncertain at this time whether a final tax reform bill with Congressional and Administration consensus can move forward quickly enough to be considered in 2017. Also uncertain at this time is whether any of the "Blueprint" or Trump proposals may be made retroactive to January 1, 2017 if passed and signed into law soon enough in 2017.

PROJECTED IMPACT

Before the November 8 elections, the House approved a number of tax bills, which will likely be part of year-end 2016 or early 2017 tax legislation. These include bills related to the IRS's civil asset seizure authority, employee stock ownership plans, and more issues as discussed below. Congress also needs to pass an omnibus spending bill to keep the federal government, including the IRS, open after mid-December 2016.

FIRST 100 DAYS

During the campaign, Trump released an outline detailing his plans for his first 100 days in office. Within his "100 day plan presentation," Trump listed several tax proposals to immediately work with Congress on enacting including:

- The Middle Class Tax Relief and Simplification Act—this legislation would provide middle class families, with two children, a 35 percent tax cut and lower the "business tax rate" from 35 percent to 15 percent. During the campaign, Trump described the plan as "an economic plan designed to grow the economy 4 percent per year and create at least 25 million new jobs through massive tax reduction and simplification."
- Affordable Childcare and Eldercare Act — A proposal described by Trump during the campaign that would allow individuals to deduct childcare and elder care from their taxable income, incentivize employers to provide on-site childcare and create tax-free savings accounts for children and elderly dependents.
- Repeal and Replace the Affordable Care Act — A proposal made by Trump during the campaign to fully repeal the ACA.
- American Energy & Infrastructure Act—A proposal described by Trump during the campaign that "leverages public-private partnerships, and private investments through tax incentives, to spur $1 trillion in infrastructure investment over 10 years."

INDIVIDUAL TAXATION

Income Tax

During the campaign, Trump proposed to compress into only three tax brackets the current seven tax brackets, which currently tops out at 39.6 percent. Trump's proposal would reduce rates on ordinary income to 12, 25, and 33 percent.

Comment:

Trump's tax plan for a three-bracket tax rate structure of 12, 25, and 33% brackets mirrors the House GOP Tax Reform Blueprint released in June 2016. Trump has not specified the income levels within which each bracket percentage would fall.

Under Trump's plan, the standard deduction would increase to $15,000 for single individuals and to $30,000 for married couples filing jointly. In contrast, the 2017 standard deduction amounts under current law are $6,350 and $12,700, respectively, as adjusted for inflation.

Trump also proposed during the campaign to implement a cap on the amount of itemized deductions that could be claimed at $100,000 for single filers and $200,000 for married couples filing jointly. Additionally, according to campaign materials, all personal exemptions would be eliminated, as would the head of household filing status.

PROJECTED IMPACT

One result of increasing the standard deduction would likely be to reduce the number of taxpayers who are eligible to claim itemized deductions.

Capital Gains/Dividends

The current rate structure for capital gains would apparently remain unchanged under Trump's plan. Trump presumably would also retain the same rates for qualified dividend income. However, Trump has proposed to repeal the 3.8 percent net investment income tax (NIIT) imposed on passive income, including capital gains.

INDIVIDUAL INCOME TAX RATES

Current Rates	Trump/GOP Rates	Joint Filers: Blueprint	Single Filers: Blueprint
10% / 15%	0% / 12%	up to $75,300	up to $37,650
25% & 28%	25%	up to $231,450	up to $190,150
33%, 35% & 39.6%	33%	above $231,450	above $190,150

PROJECTED IMPACT

The current capital gains rate structure, imposed based upon income tax brackets, would presumably be realigned to fit within Trump's proposed income tax bracket levels.

ALTERNATIVE MINIMUM TAX (AMT)

During the campaign, Trump proposed to eliminate the alternative minimum tax (AMT).

Comment:

National Taxpayer Advocate Nina Olson has recommended Congress permanently repeal the AMT. Although it serves as a revenue source, significant tax reform would likely present other options to offset the cost of elimination.

Net Investment Income Tax (NIIT)

During the campaign, Trump proposed to repeal the Affordable Care Act. Repeal of the ACA would include repeal of the 3.8 percent NIIT.

Childcare Tax Benefits

Trump proposed during the campaign to create a new deduction for child and dependent care expenses, as well as increasing the earned income tax credit (EITC) for working parents who would otherwise not qualify for the deduction. Trump's plan, as explained during his campaign, would provide:

- "Spending rebates" to lower-income families for childcare expenses through the EITC. "The rebate would be equal to a certain percentage of remaining eligible childcare expenses, subject to a cap of half of the payroll taxes paid by the taxpayer," according to campaign materials.
- "Above-the-line" deductions for child and elder care expenses, for qualified taxpayers with income up to certain thresholds.

Trump also proposed during the campaign to create Dependent CARE Savings Accounts (DCSAs), tax-favored savings accounts for children, including unborn children, and dependent care expenses, which would be matched by a government contribution. The savings accounts would have an annual contribution limit. Trump's plan would also expand the credit for employer-provided child care.

Carried Interest

Trump proposed during the campaign to tax carried interest as ordinary income.

PROJECTED IMPACT

Private equity partners have historically been taxed at 20 percent, the current top rate for capital gains.

ESTATE AND GIFT TAX

During the campaign, Trump proposed to repeal the federal estate and gift tax. The unified federal estate and gift tax takes effect at $5.49 million for 2017 (essentially double at $10.98 million for married individuals).

PROJECTED IMPACT

During the campaign, Trump also added to estate and gift tax repeal a proposal that would disallow "stepped up basis" to shelter otherwise taxable gains of more than $10 million under the current income tax law. Currently, any asset that passes through an estate receives a tax basis equal to date of death value, a significant tax advantage when the asset is eventually sold by heirs. Trump's plan would appear to provide exemptions for small businesses and family farms.

BUSINESS TAXATION

Corporate Income Tax

During the campaign, Trump proposed to lower the business tax rate to 15 percent and eliminate the corporate alternative minimum tax.

Comment:

The top corporate income tax rate is currently 35 percent.

Small Businesses

Trump's campaign materials about how pass-through entities (sole proprietorships, partnerships, and S corporations) would be taxed are broad-brushed. Generally, Trump's campaign materials indicate that the owners of pass-through entities could elect to be taxed at a flat rate of 15 percent on their pass-through income retained within the business, rather than be taxed under regular individual income tax rates (the top individual rate would be 33 percent under Trump's plan).

PROJECTED IMPACT

This plan would appear to give a business quasi-corporate status in being able to be taxed at a new 15 percent corporate tax rate until assets are distributed. Upon distribution, a second layer of tax would be imposed similar to dividends now taxed to C Corporation shareholders.

Comment:

Trump's campaign materials also indicate a consideration of rules that would prevent pass-through owners from converting their compensation income (taxed at higher rates) into profits (taxed at the 15 percent level).

Business Tax Incentives

According to campaign materials, unspecified "corporate tax expenditures" would be eliminated, except for the Research and Development (R&D) credit, in exchange for a lower corporate tax rate.

Section 179 expensing. Specifically directed toward small businesses, Trump during the campaign indicated that he would increase the annual cap on Section 179 expensing from $500,000 to $1 million.

Childcare credit for businesses. During the campaign, Trump proposed to increase the annual cap for the business tax credit for on-site childcare. Additionally, the recapture period would be reduced.

Manufacturing expensing. In lieu of deducting interest expenses, Trump proposed during the campaign that manufacturing firms would be able to immediately deduct all new investments in the business.

HEALTHCARE RELATED TAXES

Trump proposed throughout the campaign to "repeal and replace Obamacare," the Affordable Care Act (ACA), entirely, including all associated taxes. Trump's campaign materials, however, only mention repealing the ACA's 3.8 percent NII tax.

Comment:

During the campaign, Trump indicated that he would call a special session of Congress to repeal the ACA.

"Cadillac tax". Under current law, the so-called "Cadillac tax" on high dollar health insurance plans is scheduled to go into effect in 2020. Trump has not mentioned this tax specifically but repeal of the ACA would presumably include repeal of the "Cadillac tax."

Medical device tax. As part of ACA repeal, Trump's plan would apparently envision repeal of the medical device tax.

Comment:

Repeal of the ACA would also bring about repeal of the individual shared responsibility requirement, the employer shared responsibility requirement, the Code Sec. 36B premium assistance tax credit, the Health Care Marketplace, the SHOP Marketplace, and more related provisions.

INTERNATIONAL MATTERS

During the campaign, Trump indicated that one direct result of lowering the corporate income tax rate would be to make US companies more competitive worldwide, as well as keep US companies onshore.

Repatriation

During the campaign, Trump proposed to provide a deemed repatriation of corporate profits held offshore at a "one-time" reduced tax rate.

LAME-DUCK TAX LEGISLATION

Tax Extenders

A number of popular but temporary tax breaks (known as "extenders") are scheduled to expire after 2016, unless extended or made permanent by the lame-duck Congress. Energy incentives make up a good portion of these expiring incentives.

For individuals, extenders expiring after 2016 include, among others:

- Higher education tuition and fees deduction;
- Code Sec. 25C nonbusiness energy property credit;
- Mortgage debt forgiveness exclusion; and
- Mortgage insurance premium deduction.

For businesses, extenders expiring after 2016 include:

- Film, TV and live theater production expense elections;
- Mine safety equipment expense elections;
- Code Sec. 199 deduction for production activities in Puerto Rico;
- Three-year recovery for race horses; and
- Seven-year recovery for motorsports complexes.

Energy extenders expiring after 2016 include:

- Additional depreciation for second generation biofuel plant property;
- Fuel cell motor vehicle credit;
- Energy efficient commercial buildings deduction;
- Code Sec. 199 deduction for independent oil refiners;
- Credit for new energy efficient homes;
- Second generation biofuel producer credit; and
- Incentives for biodiesel, renewable diesel and alternative fuels.

PROJECTED IMPACT

The energy incentives were expected to be made permanent in year-end 2015 tax legislation. At the eleventh-hour, lawmakers decided on extending, rather than making permanent, many of the energy credits and deductions. Whether year-end 2016 tax legislation will merely extend them again or make them permanent remains to be seen. Budgetary pressures may encourage lawmakers to approve another temporary extension and punt the ultimate fate of these extenders to the new Congress in 2017.

Other Pending Tax Legislation

The "lame-duck" Congress is also expected to address a number of tax bills that were approved by the House during the summer, as well as pass an omnibus spending bill to keep the federal government, including the IRS, open into 2017. Keeping with tradition, a year-end spending bill could include tax measures.

Stock Ownership. The House passed the bipartisan Empowering Employees through Stock Ownership Bill (HR 5719) shortly before recessing in the fall. This bill would allow an employee to elect to defer, for income tax purposes, income attributable to certain stock transferred to the employee by an employer. An identical Senate bill, Sen. 3152, was introduced in July.

RESPECT Bill. In September, the House passed the bipartisan RESPECT Bill (HR 5523), which prohibits the IRS from seizing money from taxpayers who circumvent the reporting requirements unless the IRS proves that the money was connected to a crime. Similar legislation has been introduced in the Senate.

Retirement Savings. Also shortly before Congress recessed, the Senate Finance Committee unanimously passed the bipartisan Retirement Enhancement and Savings Bill of 2016, a measure that would make changes to the required minimum distribution rules for tax-favored employer-sponsored retirement plans and individual retirement accounts (IRAs).

Before year-end, some tax bills may be taken up in the House and Senate either as standalone bills or as parts of larger tax bills. A sample of these bills includes:

- The Support Small Business R&D Bill, which would expand knowledge resources available to startups and small businesses in connection with their using the research and development (R&D) tax credit.
- The Middle-Income Housing Tax Credit (MIHTC) Bill of 2016, which would provide tax credits to encourage development of affordable housing.

IRS Funding

In September, Congress approved and President Obama signed a continuing resolution to fund the federal government, including the IRS, through December 9, 2016. The continuing resolution generally funds the IRS at current levels. Not surprisingly, Congress has been unable to agree on a fiscal year (FY) 2017 budget for the IRS. As December approaches, lawmakers will likely pass an omnibus spending bill to cover all federal agencies for the remainder of the 2017 fiscal year.

CONCLUSION

The new year certainly holds the possibility of many significant changes to our current taxation structure. We will work to keep you informed over the upcoming months as to how these possible changes evolve. At Miller*Searles*, we look forward to working with you to advise you of how any changes to our current tax structure may benefit you, our clients and friends.

Very truly yours,

Miller*Searles* LLC

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