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White House unveils largely familiar tax reform principles

The Trump administration on April 26 released a one-page fact sheet outlining principles for overhauling the tax code that include, among other things, lowering the top income tax rate for corporations and passthrough entities to 15 percent, as well as shaving individual rates, compressing the rate brackets, and significantly increasing the standard deduction.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170426_1suppA.pdf

Many of the principles resemble those that then-presidential candidate Donald Trump put forward on the campaign trail in 2016. The administration did not couch its principles in legislative language, nor did it provide technical descriptions explaining how specific provisions would operate. Treasury Secretary Steven Mnuchin and National Economic Council Director Gary Cohn explained at an April 26 press briefing that the administration would develop those details in consultation with congressional leaders and release a formal proposal later this summer.

Business provisions: Significantly lower rates and a territorial tax system

On the business side, the White House is continuing with Trump's campaign pledge to lower the corporate rate down to 15 percent (from 35 percent).

Passthroughs: Also in keeping with previous campaign proposals, the plan calls for making the 15 percent rate available to businesses organized as passthroughs (that is, businesses without an entity-level tax, which currently are taxed as individuals).

Mnuchin assured reporters during the April 26 press briefing that the administration would work with Congress to develop anti-abuse rules to prevent wealthy individuals from "gaming" the tax code by recharacterizing wage income as more lightly taxed business income.

Territorial tax system: Significantly, the plan also calls for a transition to a territorial system of taxation, meaning domestic multinational businesses would only be taxed on their income connected with the US. Systems like these are much more common around the world, which explains why the fact sheet says the proposal would "level the playing field for American companies." This was likely the biggest change from the Trump campaign proposals, which called for ending deferral but otherwise retaining the current worldwide regime for taxing offshore business income of US multinationals.

Deemed repatriation: The plan repeats a call Trump made during the campaign for a one-time deemed-repatriation tax on previously untaxed earnings held overseas. The fact sheet does not cite a specific rate for the one-time levy. (The campaign proposal called for a rate of 10 percent.) When asked about this at the April 26 press briefing, Mnuchin told reporters that the administration would work with the House and Senate to determine the appropriate rate and that the rate would be "competitive."

The plan also is silent on whether the repatriation rate would be bifurcated for cash and noncash assets, or if the tax would be paid all in one year or ratably over a longer period (as proposed in the House GOP tax reform blueprint released last June and the comprehensive tax reform proposal introduced by then-House Ways and Means Committee Chairman Dave Camp, R-Mich., in 2014).

No discussion of border adjustment tax: The plan does not address whether the administration embraces the destination-based cash flow tax included in the House Republican tax reform blueprint. That proposal, which is estimated to raise over $1 trillion to help offset the cost of a proposed corporate rate cut, provides for "border adjustments" through a not-yet-specified mechanism that would serve to eliminate US tax on products, services, and intangibles exported abroad (regardless of their production location) and impose a 20 percent US tax on products, services, and intangibles imported into the US (also regardless of production location). Rival taxpayer advocacy coalitions representing export-heavy and import-heavy interests have been active on Capitol Hill recently in an effort to rally House and Senate members to their side, and there are a number of vocal skeptics of the proposal among Republicans in both chambers.

Trump, for his part, has yet to take a firm position on the proposal. In the past, he has criticized the border adjustment tax as "too complicated," and at other times he has expressed interest in the notion of an as-yet undefined "reciprocal tax" on imports.

Corporate tax expenditures: The plan proposes – without elaboration – to "eliminate tax breaks for special interests." (On the campaign trail, Trump made a similarly general call to broaden the tax base by repealing "most corporate tax expenditures.")

No infrastructure proposals: The plan does not include proposals to use any one-time revenue from business tax reform to finance new infrastructure spending. (Reports had circulated ahead of the release that President Trump might include such a proposal as a way to win support from congressional Democrats, who so far have been united in their opposition to Republican tax reform efforts.)

Individual provisions: Lower rates, fewer incentives

On the individual side, the administration proposes to provide tax relief by compressing the seven income tax rate brackets under current law (ranging from 10 percent to 39.6 percent) to three brackets of 10, 25, and 35 percent. (This is similar what Trump proposed on the campaign trail in 2016, although that plan called for a bottom rate of 12 percent and a top rate of 33 percent.) The fact sheet does not specify income thresholds for the rate brackets, however. Cohn and Mnuchin stated at the press briefing that those decisions would be finalized in consultation with congressional leaders.

Capital gains: The administration proposes to repeal the 3.8 percent tax on net investment income that was enacted under the Patient Protection and Affordable Care Act of 2010. Cohn indicated during the press briefing that the tax rate on capital gains would remain at 20 percent as under current law.

Standard deduction: The plan calls for increasing the standard deduction to $24,000 for joint filers and $12,000 for individuals, similar to a proposal in the House Republican tax reform blueprint. (During the presidential campaign, Trump called for hiking the standard deduction to $30,000 for joint filers and $15,000 for individuals.)

AMT: The plan also repeats proposals made during the presidential campaign to repeal the estate tax and the individual alternative minimum tax (AMT). The fact sheet does not mention changes to the corporate AMT.

New incentives for child care expenses: The plan includes a proposal to provide tax relief to families facing child and dependent care expenses. (Although the fact sheet does not go into specifics, Trump offered a series of proposals during the presidential campaign that called for an above-the line deduction for taxpayers facing certain child care and elder care expenses, a new tax-preferred savings account to encourage families to set aside funds for caregiving expenses, and expanded incentives for employers who offer on-site child care to their employees.)

Many current incentives targeted for elimination: The administration also proposes to simplify the tax rules for individuals by eliminating "targeted tax breaks that mainly benefit the wealthiest taxpayers." Although the fact sheet provides no details, Mnuchin and Cohn stated during their press briefing that the administration intends to snuff all current-law tax incentives *except* for those tied to the mortgage interest deduction and charitable giving. (During the campaign, Trump generally proposed to cap itemized deductions at $200,000 for joint filers and $100,000 for single filers.)

In response to a reporter's question, Cohn confirmed that the deduction for state and local income taxes is among those that are proposed to be on the chopping block.

Next steps

Mnuchin and Cohn indicated during their press briefing that White House officials intend to spend the month of May holding "listening sessions" with stakeholders and working with House and Senate leadership to refine the plan, fill in many of the technical details that are currently missing, and turn it into a formal legislative proposal. According to Mnunchin, the administration is "determined to move this as fast as we can, and get this done this year."

In a joint statement, House Speaker Paul Ryan, R-Wis., Senate Majority Leader Mitch McConnell, R-Ky., House Ways and Means Committee Chairman Kevin Brady, R-Texas, and Senate Finance Committee Chairman Orrin Hatch, R-Utah, characterized the principles put forward by the White House as "critical guideposts for Congress and the administration as we work together to overhaul the American tax system and ensure middle-class families and job creators are better positioned for the 21st century economy. …With an eye toward fairness and simplicity, we're confident we can rebuild our tax code in a way that will grow our economy, better promote savings and investment, provide our job creators with a competitive advantage, and bring prosperity to all Americans."

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