PNC CENTER FOR FINANCIAL INSIGHT

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How the Trump Tax Proposals Might Affect Planning

On April 26, 2017, President Donald Trump presented the core principles of his proposal to significantly overhaul the Tax Code. We believe that from a planning perspective it is a good time to begin considering how the most likely changes might affect existing plans.

Will a Trump presidency, buoyed by a Republican-controlled Congress, usher in a new age of tax and estate planning? And what, if anything, should the response be from a planning perspective? These are the questions on the minds of many families.

We believe now is a good time to begin thinking about what aspects of your wealth plan might be affected if key elements of the administration's tax reform proposal were passed. A wait-and-see approach is, however, most appropriate for any planning based on the proposed tax law changes, in our opinion. That being said, it is important to continue to regularly review the tax and non-tax aspects of estate plans, irrespective of the status of the current proposals. And, if you are in the process of reviewing and revising your plan, we believe that the plan changes should be finalized and executed. Further, we suggest that you work with your advisors to build flexibility provisions into your estate plan to enable future decisions and/or revisions in response to changing laws and/or circumstances.

What we do know is that President Trump has proposed a significant overhaul to the tax code. On April 26, 2017 the White House released an outline of the administration's primary goals for tax reform and National Economic Council Director Gary Cohn and Secretary of the Treasury Steve Mnuchin held a press conference to discuss it. Some specifics were provided, but a number of points still need clarification.

The Tax Code Proposal

The proposal calls for reducing individual tax brackets from seven to three, lowering corporate and individual tax rates, eliminating most income tax deductions, increasing the standard deduction, eliminating the alternative minimum tax, and repealing the estate tax (see Table 1, page 5.)

What we do not know is how these proposals will ultimately translate. While the Republicans control the House and Senate, they do not have a super majority and will likely need to work with Democrats to implement major policy changes. There are also

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likely to be changes to what is proposed, especially given the scope of the proposals and their potential impact to the federal deficit.

Estate Planning After Tax Reform

Currently, for taxable estates of more than $5.49 million (for single taxpayers) and up to $10.98 million (for married couples)[1], an estate tax of 40% is imposed. The president's plan calls for a repeal of this estate tax.

During the presidential campaign then-candidate Donald Trump, in addition to repeal of the estate tax, also proposed a capital gains tax to be imposed on appreciated assets of estates over $10 million. However, no such provision for the imposition of a capital gains tax at death was included in the president's most recent proposal. Further, his

Weighing Potential Impacts

Now is a good time to begin thinking about what aspects of your wealth plan might be affected if key elements of the administration's tax reform proposal were passed. It is, in our opinion, too early in the process to make any planning changes based on the proposals. We believe it is best to wait until something is first enacted. Below we review possible next steps if the following were to occur.

- Repeal of the estate tax: Estate planning is more than just tax planning.[2] Families utilize various tools and techniques to avoid family strife, keep family wealth in the family, pass on family values, and deter heirs from mismanaging wealth. Trusts, life insurance policies, Powers of Attorney, wills and other planning documents would need to be reviewed to ensure they align with any new tax laws and to determine if they are the best solution to meet non-tax objectives.
- Reduction of income tax rates: If your tax rate were to be lowered, it would be an opportunity to examine contributing to a Roth IRA or a Roth 401(k) and/or doing a Roth IRA conversion. There is no way to predict future tax rates, so two key considerations would be if you expect tax rates to be increased in the future or if you expect to be in a higher income bracket in retirement.
- Elimination of all but the charitable and mortgage interest deduction: Direct gifting would be one of the two ways to lower income. We believe it would be worthwhile to review how much you are directly gifting and if maximizing your deduction fits with your charitable gifting strategy.

[1] Current Estate Tax law provides that if a married taxpayer dies without fully utilizing their tax exclusion amount ($5.49 million in 2017) to which they were then entitled (for example, they pass all assets at their death to the surviving spouse via the unlimited marital deduction), the surviving spouse may elect to "port" the deceased spouse's unused exclusion amount, which they may then add to their own remaining exclusion amount to utilize for lifetime gift tax and/or estate tax purposes.
[2] For more information on the non-tax reasons for estate planning, ask your PNC advisor for our article "Using Trusts to Help and Protect You and Your Family."

proposal then, and his more recent proposal, are both silent on whether the gift tax and/or the generation-skipping transfer tax will be repealed.

The House Ways and Means Committee released a tax reform proposal in June 2016 titled "A Better Way Forward on Tax Reform." This proposal called for the repeal of the estate tax and the generation-skipping transfer tax, but did not specifically address the current step-up in basis rules at death or the potential repeal of the gift tax. It appears that the president and the Republicans in the House agree that the estate tax should be repealed, but they may not be in complete agreement when it comes to treatment of all of the other current transfer tax provisions.

"The president's plan proposes to eliminate all itemized deductions with the exception of the deduction for charitable gifts and the mortgage interest deduction. Should the final legislation enact such changes, these two remaining deductions may become valuable tax reduction tools."

Will Income Tax Planning be the New Estate Tax Planning?

If the estate tax is repealed, trusts established for estate planning purposes will need to be reviewed. Trust-owned life insurance policies will also need to be reviewed to determine the best options considering the specifics of the final tax reform legislation. Finally, with the federal government no longer taking a portion of the estate, affluent families will have a greater opportunity to make charitable bequests.

The individual tax proposals could potentially have a large impact on overall tax planning. In addition to collapsing the individual brackets, President Trump proposes to eliminate the alternative minimum tax (AMT), the net investment income tax, and the head of household filing status. The proposed tax plan also doubles the current standard deduction, and introduces child-care-related tax provisions, such as making child-care costs deductible from adjusted gross income for most Americans up to the average cost of care in their state (phased out at income over $250,000 for single and $500,000 for married filed jointly).

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Businesses Look Set to Benefit

President Trump's tax plan would reduce the corporate rate from 35% to 15% and simplify the tax code. The proposal does this by eliminating the corporate AMT, the domestic production activities deduction, and all other business credits with the exception of the research and development credit. A key element to the president's proposal was to allow pass-through business entities to take advantage of the lower rates as well as larger corporations. Finally, the president proposed a one-time tax on overseas profits held by U.S. businesses, although the specific tax rate was not provided.

The House "A Better Way" Plan Might Be a Stronger Indicator of Tax Changes to Come

The Republicans in the House of Representatives have been working on their own tax proposal that might shed some light on the potential form of any changes to the tax regime in 2017. On June 24, 2016, House Republicans introduced what is known as the "A Better Way" tax plan. The plan is based on three pillars and has many similarities to Mr. Trump's tax plan.

The pillars are simplicity and fairness, jobs and growth, and an Internal Revenue Service (IRS) that makes service its first priority. According to Speaker Paul Ryan's website, the plan seeks to make the tax code simpler for all taxpayers, to make it easier to create jobs, and to create a fairer IRS that puts the taxpayer first. Areas where the two plans align are thought to have a higher probability of becoming law although they will need additional support to pass. The two plans align on the following points:

- condensing the code to three tax rates: 10%, 25%, and 35%;
- eliminating itemized deductions with the exception of mortgage interest and charitable contributions;
- doing away with personal exemptions;
- raising standard deductions, although the amounts in the plans are different;
- jettisoning the AMT;
- ridding the surtax on net investment income;
- lowering the corporate tax rate, with Mr. Trump's plan calling for 15% and the A Better Way plan, 20%; and
- eliminating the estate tax.

Table 1

2017 Current Tax Law versus Trump Tax Proposal

Current 2017				Trump Proposal	
Single Individuals		**Married**		**Single Individuals**	**Married**
Not over $9,325	10%	Not over $18,650	10%	10%	10%
$9,325 - $37,950	15%	$18,650 - $75,900	15%		
$37,950 - $91,900	25%	$75,900 - $153,100	25%	25%	25%
$91,900 - $191,650	28%	$153,100 – $233,350	28%		
$191,650 - $416,700	33%	$233,350 – $416,700	33%	35%	35%
$416,700 - $418,400	35%	$416,700 - $470,700	35%		
Over $418,400	39.6%	Over $470,700	39.6%	Income Brackets not Provided	

Capital Gain & Dividend Tax		Capital Gain & Dividend Tax	
If Income Tax Bracket is:	Capital Gain and Dividend Rate is:		
15% or less	0%	0%	
25%, 28%, 33%, or 35%	15%	15%	Income Brackets not Provided
39.6%	20%	20%	

Net Investment Income Tax	Net Investment Income Tax
3.80% on the lesser of: 1) Net Investment Income 2) Excess of modified adjusted gross income over: $200,000 for single taxpayers $250,000 for married taxpayers filing jointly	ELIMINATED

Standard Deduction		Standard Deduction	
Single:	$6,350	Single:	$12,700
Married Filing Jointly:	$12,700	Married Filing Jointly:	$25,400

Itemized Deductions		Itemized Deductions
Single – Phase-out starts at AGI of:	$261,500	Eliminate All Deductions Except Charitable and Mortgage Interest Deductions
Married – Phase-out starts at AGI of:	$313,800	

Alternative Minimum Tax		Alternative Minimum Tax
Single Filer Exemption Amount:	$54,300	ELIMINATED
Married Filing Jointly Exemption Amount:	$84,500	

Business Income Taxes

Current 2017		Trump Proposal	
Corporate Income Tax Rate:	35%	Corporate Income Tax Rate:	15%
Pass-Through Business Entities:	Individual Tax Rate	Pass-Through Business Entities:	15%
Carried Interest:	Capital Gain Rate	Carried Interest:	Ordinary Income Tax Rate

Estate & Gift Taxes

Current 2017		Trump Proposal	
Estate Taxes		**Estate Taxes**	
Individual Unified Credit:	$5.49 Million	ESTATE TAX REPEALED	
Married Unified Credit (Portability)	$10.98 Million	Basis After Death:	Fair Market Value at Date of Death
Estate Tax Rate:	40%		
Basis After Death:	Fair Market Value at Date Of Death	Note: During campaign Trump proposed to eliminate "step-up" in basis rules for estates over $10 million (married). Not mentioned in 2017 proposals to date.	
Gift Taxes		Gift Taxes	
Individual Unified Credit:	$5.49 Million	Not mentioned in 2017 proposal	
Married Unified Credit (Portability)	$10.98 Million		
Estate Tax Rate:	40%		

For more information, please contact your Hawthorn advisor.