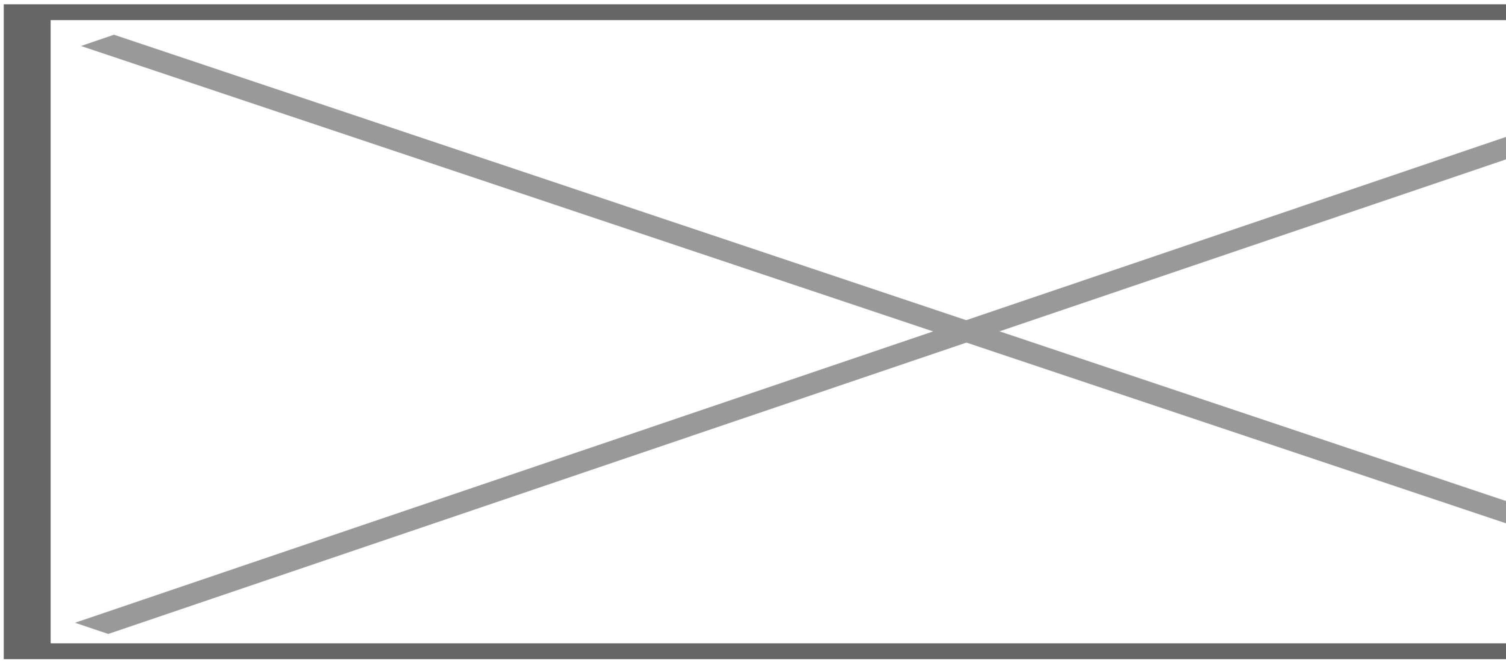
US Tax under Trump – Reduce, repeal and simplify?

International Tax Tax voice



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David Treitel provides a view on the future and a recommendation to act sooner rather than later

US tax reform in 2017? Yes or No? Aside from nudging clients to get ready for significant change; the tough thing speaking to anyone about US tax reform today is that all the issues mentioned to date seem to be broadly outlined, light in detail and seemingly based on no more than plentiful tweets. The over-arching theme of the Trump administration has nonetheless emerged clearly. *Reduce, repeal and simplify*. Based on this limited set of policy objectives, this article highlights the safest individual US tax planning tools available today; accelerate or defer.

Reduce?

Trump has kindly promised that we should soon be seeing "phenomenal" tax reform throughout the US tax system. On the individual tax front, Trump talked throughout the campaign last year of simplifying the current seven US tax brackets to just three rates set at 12%, 25% and 33%; the lowest of which is higher than the current lowest rate of 10% and the highest lower than the current highest of 39.6%. Trump has also talked of raising the standard deduction to $15,000 per person.

Repeal?

Trump has also spoken frequently of dismantling the Affordable Care Act (commonly known as Obamacare). To this end, he issued an Executive Order in January permitting the IRS to process individual tax returns even if the return does not indicate whether a taxpayer had health insurance. It seems, therefore, a likely outcome that the 3.8% Net Investment Income Tax (NIIT) surcharge on wealthier taxpayers, designed in 2010 to pay for Obamacare, will be eliminated by the end of 2017. Trump has also proposed to repeal personal exemptions and eliminate the Alternative Minimum Tax (AMT).

There are also strong indications that Trump continues to intend to repeal the estate tax, although its replacement might include a capital gains tax for estates over certain thresholds.

Simplify?

While detailed tax policy proposals are not expected until the full budget, expected to be released around May, the President released a preliminary spending budget for 2018 in March 2017 called "*America First: A Budget Blueprint to Make America Great Again*". This budget mainly made the headlines by arguing for a $52 billion increase in defence spending; but contained no detailed tax proposals at all (unless one includes a commitment to reduce the IRS spending budget by $239 million).

Although a reduction in the number of tax rates and an increase in the standard deduction could reduce tax for many individuals; it seems inevitable with any major change that some groups of taxpayers might be worse off.

No News? Good News?

Although there is no draft legislation confirming future tax rates or indicating when any tax reform might be implemented, clients will naturally still want to know how they can best plan their finances for unknown and unpredictable tax changes. With few details yet available, the best tax planning today relies on the traditional techniques of *accelerate or defer*. Based on the decently strong assumption that tax rates overall will reduce, especially at the higher levels, it could make sense for many clients to delay income or gains until rates are lower. Equally clients may want to arrange to pay and claim expenses currently while tax rates are higher.

Accelerate or defer?

While US tax rates are seemingly higher now than they are likely to be in the future, a US person might as mentioned above think of accelerating revenue and capital expenses to get tax relief at today's higher tax rates. Equally, it could be helpful to realise capital losses currently so that these can be offset against gains taxed at today's capital gains tax rates. Some clients may want to pay foreign (e.g. UK) tax earlier, in case foreign tax credits are of lower value or use in the future.

Within these broad themes, some clients will have specific opportunities today. For example, because of the sharp fall in the Pound over the past year, US individuals who have UK investment portfolios which show capital gains when expressed in Sterling might want to review their investment portfolios to see if any of the same valuations might result in dollar losses that could be realised at today's US tax rates. The fall in the Pound also presents an opportunity for many Americans in the UK to sell a broad range of investments that might not be considered "US tax friendly"; such as most UK unit trusts, investment trusts and OEICs (these are generally unsuitable for US persons from a tax perspective, because of the anti-avoidance "Passive Foreign Investment Company" rules). While exploiting the fall in the Pound to save tax might appear unconventional tax advice, many Americans in the UK have historically held investments directly and within ISAs and Junior ISAs without adequate consideration of US tax consequences.

For anyone in the UK who wants to avoid all US tax changes by renouncing US citizenship, the fall in the Pound over the past year has reduced the Sterling equivalent of the expatriation tax threshold of $2 million, making it easier for some individuals to expatriate free of a possible US tax charge.

Deciding to defer income or gains is a seemingly obvious choice if tax rates are likely to be lower in the future. At the most extreme end; some people may choose to delay the date of a relative's death by extending life-support until after the estate tax has been abolished. (While keeping grandad on life-support may not be something typically discussed in ADIT Voice, changes in mortality rates based on expected reductions in the rate of tax on death have been observed in the past; economists even have a fancy phrase for the effect, calling it "death tax elasticity".)

More practically, aiming to delay anything that triggers the AMT, such as exercising US qualified incentive stock options, could be prudent as might delaying anything that is likely to be subject to the NIIT; which includes delaying realising capital gains as rates might be lower in the future. For taxpayers with non-US dollar mortgages, delaying paying off capital could also save money; as the US tax rate on foreign currency gains seems likely to be lower in future.

Change? Yes! Now

In a world where no-one can predict future tax policy, using rules that exist today seems to be the best and most pro-active client advice available. Plan for change, but starting changing your client's plans sooner than later.