



Projected Post-Election Changes to Income and Estate Tax Laws

BY ROBERT J. KOLASA

Given his unfavorable polling numbers and countless campaign gaffes, many (especially those residing in “blue states” such as Illinois) thought that Donald J. Trump had little chance of winning the recent Presidential election.

But, surprisingly, the New York businessman won the election. The cherry on top for Republicans was that they also obtained majorities in the U.S. Senate and House of Representatives. The political significance of controlling all legislative branches makes Republican-style tax reform a virtual certainty in 2017.

INCOME TAX CHANGES

Although it is hazardous to predict future tax legislation, the following proposals seem likely to become law, in one form or another, since they appear in the Trump/Pence “Make America Great Again” website¹ (i.e., the “Trump Plan”):

- **Restructuring of Individual Income Tax Rates.** Today, there are seven different regular tax brackets for individuals, with a top individual income tax rate of 39.6% (plus the additional 3.8% “Medicare surtax”). The Trump

Plan will collapse these brackets to the following three brackets for married joint filers (brackets for single filers are one-half of these amounts):

Less than \$75,000: 12%
More than \$75,000 but less than \$225,000: 25%
More than \$225,000: 33%

- **Other Rate Changes and Repeal.** The existing capital gains rate structure, with a maximum rate of 20%, is retained. However, the alternative minimum tax (“AMT”) and 3.8% Medicare surtax are repealed.

- **Itemized and Standard Deductions.** For married joint filers, (1) itemized deductions are capped at \$200,000; and (2) the standard deduction is increased to \$30,000. For single filers, the limits are one-half of these amounts. The personal exemption (currently \$4,050 for taxpayers and their dependents) is eliminated, along with the head of household filing status.

- **Childcare and Eldercare Deduc-**

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¹ <https://www.donaldjtrump.com/policies/tax-plan/>

tions. Taxpayers will have a new “above-the-line” deduction for up to four children under age 13, capped at the average cost of care for the state of residence. The precise method to determine the capped limits has not been announced, but presumably it will be based on an ascertainable index. For children taking care of elderly dependent parents, a similar “eldercare” deduction (capped at \$5,000, adjusted for inflation) is also available. These deductions are not available for married joint filers making over \$500,000 (\$250,000 for single filers). The Trump Plan also offers child care spending rebates to lower-income taxpayers through the existing earned income tax credit.

• **Dependent Care Savings Accounts.**

The Trump Plan creates new Dependent Care Savings Accounts (DCSAs) so that families can set aside extra money (\$2,000 per year contribution limits) to foster their children’s development and offset elder care

for their dependent parents. Presumably these new accounts will allow both tax-deductible contributions and tax-free appreciation. When the child reaches 18, additional contributions are not allowable but DCSA funds can be used for educational expenses. To encourage lower-income families to establish DCSAs for their children, the government will provide a 50 percent match on parental contributions of up to \$1,000 per year for these households.

- **Generous Business Income Tax Provisions.** The Trump Plan lowers the business tax rate from 35 percent to 15 percent, and eliminates the corporate alternative minimum tax. This rate is available to all businesses, both small and large, that want to retain the profits within the business. Most corporate tax subsidies, other than the research and development credit, would be eliminated. Firms engaged in manufacturing have the option to expense capital investments, but lose the deductibility of corporate interest expense. Significantly, the plan provides for a deemed repatriation of corporate profits held offshore at a one-time tax rate of 10%.

ESTATE TAX REPEAL

The Trump website provides the following cryptic statement regarding estate tax repeal: “The Trump Plan will repeal the death tax, but capital gains held until death and valued over \$10 million will be subject to tax to exempt small businesses and family farms.”

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Many commentators construe the above language to signify implementation of a “Canadian-style” approach, replacing the federal estate tax with a deemed capital gains tax at death for estates over \$10 million. On a simplistic level, this can be seen as substituting the 20% capital gain rate for the more expensive 40% estate tax rate. So ironically, under the Trump Plan there may still be an “estate tax,” in that a tax would be triggered at death, but it just wouldn’t be called that.² Under this system it would be more productive to have senior family members hold high basis assets to lessen capital gains (reversing the current strategy of such members holding low basis assets to obtain “stepped-up basis”).³

For larger estates, much of the same planning as is done today would probably continue (i.e., discount driven techniques in which planners attempt to shift wealth to younger generations). For “smaller” estates under \$10 million, such measures could be disastrous. For example, under current valuation discount rules it is generally possible to contend that \$5 million

of assets contributed to a “properly drafted” LLC are worth \$4 million on a post-contribution basis. The \$1 million difference magically disappears from the estate tax system, although without estate taxes, more income taxes may be triggered since the disappearing \$1 million of asset value is not eligible for stepped-up basis.

On the other hand, the Trump Plan may eventually evolve to repeal the estate tax by adopting a “carryover” basis system. Under this method, there is no immediate tax upon death but assets over some threshold (\$10 million?) do not qualify for stepped-up basis, thereby generally deferring income taxes until such assets are sold. This type of system was adopted in 2010 during that strange one-year hiatus where the estate tax was temporarily repealed for estates electing into this system. It is noted that Trump’s former nemesis (but now pal), House Speaker Paul Ryan, seems to support some variation of this approach in the comprehensive tax reform package he and fellow Republicans developed during the campaign.⁴

Whatever rules are adopted, numerous uncertainties

2 LISI Estate Planning Newsletter #2480 (November 16, 2016) at <http://www.leimbergservices.com>.
 3 “Stepped-up basis” generally refers to the basic adjustment under IRC 1014 whereby assets includible in the client’s gross estate at death receive a basis increase to fair market value at date of death. Effectively, this means that the pre-death appreciation is forgiven. Assets not qualifying for stepped-up basis are sometimes referred to as “carryover basis” assets, in that the basis of such assets are not adjusted at death.
 4 “A Pro-Growth Tax Code for All Americans” at https://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf.

will abound on the practical aspects of implementing estate tax repeal. Under a deemed capital gains tax system, would the stepped-up basis rules still be applicable for the first \$10 million of exempt asset value? Will the gift tax system be retained as a “backstop” to preserve the integrity of the income tax system, to avoid gifting of assets to family members in lower tax brackets? What will happen to the estate tax marital deduction, small business/farm deduction, charitable deduction and generation skipping transfer tax? Under any post-repeal system, it would seem that the tracking of asset basis would be an integral component of compliance and planning.

For Illinois estates, the \$64,000 question is whether the Illinois legislature will repeal the existing Illinois estate tax in light of federal estate tax repeal (under its statutory language, the Illinois estate tax seems to stand intact irrespective of federal repeal).⁵ One can just hear the sucking sound of jobs and wealth leaving our beloved state if somehow the Illinois estate tax is retained. Given our peculiar history of legislative gridlock, this may be a real possibility.

Finally, the strong likelihood of estate tax repeal has caused more than a few estate planners to worry about job security once the word “estate taxes” are taken out of their job description. However, the consensus opinion is that

competent tax advice will always be worthwhile to clients once the new rules are finalized. The game has merely changed, not the planner’s participation in the game. The challenge is not to dwell in the past and dynamically embrace the new rules as a business opportunity. Thankfully, there should be an immediate short term spike in business as most estate plans will have to be reviewed to see if they optimally mesh with the new law.

PAYING FOR THE TAX CUTS

The Trump Plan is not a pay-as-you-go system, as spending cuts will not be earmarked to pay for it. A recent article in *The Wall Street Journal* estimates that Mr. Trump’s tax and spending proposals will increase the federal deficit to 6.8% of gross domestic product (from the current 3.2% level) by the end of his first term.⁶ So much for fiscal restraint. However, Mr. Trump and his proponents forcefully contend that their policies will strengthen the economy by creating jobs and increasing GDP growth to new robust levels. We all hope Mr. Trump is correct and that his policies will indeed supercharge our economy. Nevertheless, if deficits are not reigned in, meaningful entitlement reform will likely need to be addressed by future administrations.

5 35 ILCS 405/1, et. seq.

6 Nick Timiraos, *Trump’s Fiscal Plan Roils GOP*, *The Wall Street Journal*, November 28, 2016, at A3.

ACCESS TO JUSTICE AWARDS

Nomination Deadline Friday, January 27, 2017

Presentation of Awards, Tuesday, March 14, 2017

Membership Luncheon, Waukegan City Hall

Access to Justice Award: A Lake County Bar Association member who has provided or supported legal services to low-income clients, and who has made a particularly significant or meaningful contribution to the provision of low-income legal services.

Gideon’s Award: An attorney who is employed or retained by a public or non-profit agency to provide criminal legal services to low-income clients, and who has made a particularly significant or meaningful contribution to the provision of low-income legal services above and beyond the requirement of his or her position.

Robert H. Jackson Award: A prosecutor who has distinguished himself or herself in public service, and whose commitment to justice and serving the communities where he or she lives or works, is particularly praiseworthy. The nomination should address the individual’s outstanding characteristics, prosecution history, work with the public and contributions to the quality of prosecution and the image of prosecutors.

*Nomination forms available at www.lakebar.org, calendar,
Access to Justice Awards Luncheon, March 14, 2017*