MILLER, MONSON, PESHEL, POLACEK & HOSHAW

A PARTNERSHIP OF PROFESSIONAL LAW CORPORATIONS

OCTOBER 2016 NEWSLETTER

501 WEST BROADWAY, SUITE 700
SAN DIEGO, CALIFORNIA 92101-3563
TELEPHONE: (619) 239-7777
FAX NUMBER: (619) 238-8808

IN THIS ISSUE

A COMPARISON OF PRESIDENTIAL CANDIDATES' TAX PLANS

by DeEtte L. Loeffler, J.D., LL.M. Taxation

It is difficult in this current environment to obtain truly neutral analysis of anything, including the tax proposals of the leading presidential candidates, Hillary Clinton and Donald Trump. The Tax Policy Center has been accused of using "old modeling" that supports Democratic positions, while the Tax Foundation has been accused of using modeling designed to support the Republican positions. Modeling, as you know, is an imperfect science because it requires the modeler to use assumptions about how individuals and businesses will respond to increases in taxes, decreases in taxes, the introduction of new taxes, and/or the elimination of old ones. This article is intended to be neutral, but we cannot guarantee the accuracy of the information on which it is based. Information has been collected from the Tax Policy Center, the Tax Foundation, and the public websites of both candidates. We hope this information is helpful to you.

The Clinton Tax Plan

According to her website[1], Hillary Clinton is proposing a tax system in which all Americans pay a "fair share" of the taxes. Change would include:

1. Adopting the "Buffett Rule" to impose a minimum rate of 30% on those earning $1 million or more annually and imposing a 4% "fair share surcharge" on 20% of all taxpayers earning $5 million or more annually;
2. Capping additional contributions to high value retirement plans (the "Romney Loophole");
3. Taxing "carried interest" at ordinary income rates;
4. Decreasing the estate tax exemption to $3.5 million (from $5.45 million currently), increasing the rate to 45% (from 40%), and imposing a graduated rate schedule of up to 65% on estates over $1 billion;
5. Imposing an "exit tax" on companies moving their headquarters overseas (i.e., on inversions) and prohibiting earnings stripping by companies already located outside the US;
6. Ending oil and gas subsidies;
7. Creating a standard deduction for small businesses, allowing investment expensing and increasing deductions for start-up costs;
8. Making "excessive" health care and elder care expenses deductible.

Although not mentioned on her website, Ms. Clinton would also impose a graduated capital gains tax rate of 24% to 39.6% on "medium term" investments held more than one, but less

[1] https://www.hillaryclinton.com/issues/a-fair-tax-system/

than six, years.[2] She would also limit the value of exemptions and deductions to 28% for high income earnings[3], and would modify the grantor trust rules to prevent income shifting.[4]

According to the Tax Foundation, her plan would result in a net increase in revenues of $191 billion over the next decade, and reduce the gross domestic product (GDP) by 1 percent, resulting in 0.8 percent lower wages and 311,000 fewer full-time equivalent jobs.[5]

According to the Tax Policy Center, her plan would increase revenue by $1.1 trillion over the next decade, with nearly all tax increases falling on the top 1.0% of earners. It would also decrease the federal deficit by $4.3 trillion by 2036.[6]

Trump Tax Plan

According to his website[7], Donald Trump is proposing the following changes to the federal tax system:

1. Collapsing the current seven (7) tax brackets into three (3): 12% (for those earning up to $75,000), 25% (for up to $225,000) and 33% (for those over $225,000);
2. Repealing the 3.8% Net Investment Income Tax (NIIT)
3. Taxing “carried interest” as ordinary income;
4. Eliminating all personal exemptions, increasing the standard deduction to $15,000 per taxpayer (from $6,300), and capping itemized deductions at $100,000 per taxpayer;
5. Repealing the estate tax, but imposing capital gains tax on assets at death (excluding the first $10 million). Also prohibiting gifts at death to private charities (established by taxpayer or relatives);
6. Reducing the corporate tax to 15% (from 35%) and eliminating the AMT on business;
7. Imposing a 100% one-time tax on unrepatriated corporate earnings kept off shore;
8. Eliminating more corporate expenditures, except Research and Development, and allowing corporations to elect to expense investments instead of deducting them.

Although not mentioned on his website, Mr. Trump will also repeal the federal gift tax and repeal the individual AMT.[8]

According to the Tax Policy Center, his plan would cut taxes for all taxpayers, but the highest cuts would go to high income earners. It would reduce tax revenues by $9.5 trillion over the next decade. Two-thirds of the anticipated revenue loss would come from reduced individual income taxes and one-third from cuts to the corporate tax.[9]

According to the Tax Foundation, his plan would decrease tax revenues by a net $10.14 trillion over the next decade, but result in higher interest payments for the national debt. Assuming the tax cuts can be financed, it would increase GDP by 11.5% over the long term and lead to 29% larger capital stock, 6.5% higher wages, and 5.3 million more full-time equivalent jobs.[10]

While tax plans are just that, plans, it appears clear from the information above that significant changes may be implemented in the next presidential term. We will continue to keep you informed as we identify proposals that may impact you, your families, and your business.

---

[2] http://taxfoundation.org/comparing-2016-presidential-tax-reform-proposals

[3] The cap would apply to all itemized deductions, (except charitable contributions, which are already capped at 30% or 50% of AGI), exempt interest, excluded employer provided health insurance, and deductible contributions to tax preferred retirement accounts.

[4] http://www.taxpolicycenter.org/publications/analysis-hillary-clintons-tax-proposals/full

[5] http://taxfoundation.org/sites/default/files/docs/TaxFoundation-FF496.pdf

[6] http://www.taxpolicycenter.org/publications/analysis-hillary-clintons-tax-proposals/full

[7] https://www.donaldjtrump.com/positions/tax-reform

[8] http://www.taxpolicycenter.org/publications/analysis-donald-trumps-tax-plan/full

[9] Id.

[10] http://taxfoundation.org/article/details-and-analysis-donald-trump-s-tax-plan

IRS WILL NOT CHALLENGE AQ TRUSTS

by DeEtte L. Loeffler, J.D., LL.M. Taxation

Revenue Procedure 2016-49, a highly anticipated ruling, was released September 27, 2016. The IRS has announced it will not challenge QTIP elections made for trusts when the election is not *required* in order to reduce the decedent's taxable estate so long as the estate also makes a portability election under IRC Section 2010(c)(5)(A). This is good news for estate planners and their clients who will no longer run the risk of having their preferred planning disregarded.

The ruling ends a controversy which began with the advent of portability in 2011. Beginning with 2011, the executor of the estate of a deceased married person has had the power to claim the unused portion of the deceased spouses' unused exemption from the estate tax ("portability") for use by the surviving spouse. This "deceased spousal unused exemption amount" (DSUEA) can be used by the surviving spouse to exempt lifetime gifts from the federal gift tax and to exempt transfers at death from the federal estate tax.[11]

Attorneys were quick to see the potential income tax advantages which portability can provide to families. Assets taxable in the estate of the surviving spouse are permitted a new fair market value basis upon the surviving spouse's death.[12] For many families, portability (coupled with the rising exemption from the estate tax under IRC Section 2010) reduced or eliminated the risk that the survivor's estate would have to pay an estate tax. With portability, the first spouse to die could now afford to leave all of his or her assets to the surviving spouse and obtain a new income tax basis to benefit the couple's children or other heirs.

However, not all spouses wanted such "simple" planning, especially in blended families where the surviving spouse was not the parent of all of the deceased spouse's children. As a response to this situation, attorneys conceived the idea of funding a martial exemption or QTIP (qualified terminable interest property) trust to receive the assets of the first spouse to die. Since the assets in a QTIP trust are taxable in the estate of the surviving spouse, but the survivor does not have ownership of the assets so cannot change the ultimate beneficiaries, this "AQ" or "AQB" planning provided an acceptable option.

There remained, however, a risk that the IRS would disregard the QTIP election if the election was not required in order to prevent a tax in the estate of the first spouse to die. In a taxpayer-friendly ruling in 2001, Revenue Procedure 2001-38, the IRS had advised taxpayers that if an estate made a marital election and the election was not required in order to reduce the taxable estate, the IRS would disregard the election. This ruling benefitted taxpayers who mistakenly made the election and, as a result, might then owe an estate tax at the death of the surviving spouse because too many assets would be subject to tax in the survivor's estate. Some attorneys were concerned the IRS might use this revenue procedure as a sword to deny the marital election and cause the QTIP Trust to be treated like a bypass trust (and so not be entitled to a basis step-up). To counter this risk, some attorneys were recommending clients make a "partial QTIP election" allowing some assets to also fund a bypass trust on the assumption that such a partial election would remove the client's estate tax return from the category of estates covered by 2001-38.

Revenue Procedure 2016-49 eliminates this concern. The IRS has stated that it will continue to make use of Rev. Proc. 2001-38 in appropriate cases to benefit a taxpayer who made an inadvertent marital election. However, if the taxpayer also elects portability of the DSUEA on the same estate tax return, the IRS will honor both elections. Trusts designed to fund a marital trust at the first death (regardless of the size of the estate) will now be safe making the marital and portability election

[11] IRC Section 2010(c).
[12] IRC Section 2014.

without the need to also partially fund a bypass trust.

FEDERAL TAX NEWS

by DeEtte L. Loeffler, J.D., LL.M. Taxation

Financial Aid Filing Starts Three Months Early. The filing date for the Free Application for Federal Student Aid (FAFSA) starts on October 1, 2016. The filing period usually begins on January 1st, but the government has decided to give students a longer time period to apply for financial assistance. In order to potentially receive grants and loans in 2017, students must provide information from the 2015 or 2016 tax year. The deadline to file is June 30, 2017.

Private Collection Agencies to be Pursuing Federal Tax Debt. Starting next spring, the IRS will no longer be actively working on accounts that owe federal taxes. Four private collection agencies have been selected to take over these accounts. Under the Fair Debt Collection Practices Act, these contractors will be required respect the rights of taxpayers. These companies will not take any money personally. They are required to direct people to pay overdue taxes online at www.IRS.gov or send checks made payable to the U.S. Treasury directly to the IRS. Taxpayer advocates have expressed concerns that private bill collectors will not work cooperatively with taxpayers to settle debts.

Congress Ready to Reduce Taxes - on Beer. Craft brewers and small batch producers are likely to see a reduction of their excise taxes under two bills advancing through Congress (S. 1562 and HR 2903). As of September 26, 2016, the bills have sufficient support to pass. Under the change, the excise tax imposed on a barrel of beer would drop for US brewers from $7.00 to $3.50 for the first 60,000 barrels, and would drop from $18.00 to $16.00 per barrel for other brewers and importers.

STATE TAX NEWS

by DeEtte L. Loeffler, J.D., LL.M. Taxation

Continued Higher Taxes Appear Likely for the Wealthy. When California adopted a 1.0% tax increase on high income earners in 2012, the change came with a promise by Governor Brown that the tax increase would end after 2016 and that all taxpayers would share in at least some of the tax burden. Now those promises look likely to be broken, although not by Governor Brown (who resisted legislative efforts to extend the tax). Proposition 55, which is on the November ballot, would allow the *sales tax* burden to decline from 7.5% back to 7.25% (the part of the tax increase that applied to everyone) while extending the tax on those with income in excess of $250,000 through the year 2028. The tax proceeds would be applied to schools (K-12), community colleges (11%), and Medi-Cal and other health care services ($2 billion).

Tax Relief for Disaster Victims. The State Board of Equalization now has increased authority to defer collection of taxes from businesses impacted by “disasters” where good cause is shown. AB 1559, which was signed into law in September, increases the BOE’s authority to defer business tax payments without imposing additional costs or fees on the taxpayer from 1 to 3 months and broadened the definition of when this power may be exercised.

Governor Vetoes Diaper Tax Bill. In an attempt to balance the budget, Governor Jerry Brown decided to veto Assembly Bills 1561 and 717 which would have repealed sales taxes on diapers and feminine hygiene products. This action has outraged many advocacy groups, because less “essential products” (such as candy) are exempted from sales tax. Governor Brown justified his actions in individual veto messages. The primary reason was that California would lose $45 million in revenue if these two bills became law.

Disclaimer: This newsletter is provided to share knowledge and expertise with our colleagues with the goal that all may benefit. The content of this newsletter is for general informational purposes only.

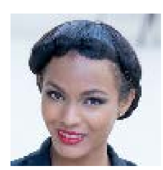
The information contained within this newsletter is not intended to serve as legal advice or as a guarantee, warranty or prediction regarding the outcome of any particular legal or tax matter. Nothing contained within this newsletter should be used as a substitute for legal advice and does not create an attorney-client relationship between the reader and Miller, Monson, Peshel, Polacek and Hoshaw. Legal advice depends on the specific facts and circumstances of each individual's situation. You should not rely on this newsletter without first consulting with a qualified, licensed attorney.

MILLER, MONSON, PESHEL, POLACEK & HOSHAW

A Partnership of Professional Law Corporations
Providing quality legal services since 1959

RALPH GANO MILLER, RETIRED
THOMAS M. MONSON
MARY J. PESHEL
TIMOTHY C. POLACEK
WILLIAM D. HOSHAW†
SUSAN L. HORNER
DeETTE L. LOEFFLER
BRADFORD N. DEWAN
JUDY S. BAE
PHILIP R. FREDRICKSEN†
†OF COUNSEL

http://www.mmpph.com



Editor and Co-Writer: Marica L. Sutton, BA, Communication, University of Louisville, 2011