GMS Flash Alert

2017-157 | November 2, 2017

United States – House Republicans Unveil Tax Reform Bill

On November 2, 2017, U.S. House Ways and Means Committee Chairman Kevin Brady (R-TX) unveiled a much anticipated House Republican tax reform bill, entitled the Tax Cuts and Jobs Act ("the TCJA").[1] The draft legislation, a major step forward in the tax reform process, offers the public its first glimpse at proposed statutory language and provides an opportunity to consider the impact of tax reform on assignees and international assignment programs.

The TCJA proposes significant tax cuts for middle-class individual taxpayers, and also cuts the corporate tax rate from 35 percent to 20 percent. This alert will focus on some of the TCJA's proposed changes affecting individual taxpayers, specifically those that affect Global Mobility programs. Unless specifically indicated below, the changes proposed by TCJA would be effective for tax years beginning after 2017.

WHY THIS MATTERS

If enacted, the TCJA would represent the most comprehensive reform to the U.S. tax code in over thirty years and would have a dramatic impact on international assignment programs.

The proposed changes to the individual income tax rates would affect the overall cost of equalized assignments to and from the United States. U.S. outbound assignments could be more expensive for employees whose U.S. hypothetical tax offset would be lower. Conversely, U.S. inbound assignments could be less expensive, as the actual U.S. tax cost for an employer would be lower. However, outcomes will vary depending on each taxpayer's specific facts.

Additionally, the proposed changes to itemized deductions will change tax equalization calculations that determine stay-at-home tax using hypothetical tax itemized deductions. Changes to taxation of home sales and elimination of the moving expense deduction may also have an impact on program costs and policy provisions.

Multinational employers with globally mobile workforces should consider reviewing their global mobility policies in light of these proposed changes.

Key Provisions of the TCJA

Ordinary Individual Tax Rates

The TCJA would reduce the number of federal income tax brackets from seven (ranging from 10 to 39.6 percent) to four for ordinary income: 12, 25, 35 and 39.6 percent. For individual taxpayers, depending on their filing status, the tax brackets applicable to income in excess of the specified thresholds would be as follows:

2018		Proposed	
	Single		Single
Tax Rate	If taxable income is:	Tax Rate	If taxable income is:
10%	$9,525	12%	$0 to $45,000
15%	$9,526 to $38,700		
25%	$38,701 to $93,700	25%	$45,001 to $200,000
28%	$93,701 to $195,450		
33%	$195,451 to $424,950	35%	$200,001 to $500,000
35%	$424,951 to $426,700		
39.60%	$426,701 or more	39.60%	$500,001 or more

2018		Proposed	
	Married Filing Joint		Married Filing Joint
Tax Rate	If taxable income is:	Tax Rate	If taxable income is:
10%	$19,050	12%	$0 to $90,000
15%	$19,051 to $77,400		
25%	$77,401 to $156,150	25%	$90,001 – $260,000
28%	$156,151 to $237,950		
33%	$237,951 to $424,950	35%	$260,001 – $1,000,000
35%	$424,951 to $480,050		
39.60%	$480,051 or more	39.60%	$1,000,000 or more

KPMG NOTE

The overall effect of these changes to the tax rates and thresholds is to slightly expand the number of people falling into the 25 percent bracket, significantly expand the number of people falling into the 35% bracket (due to significantly lower threshold for 35 percent), and significantly reduce the number of people falling into the 39.6 percent bracket (particularly for married taxpayers filing jointly for whom the threshold at which the highest rate of tax applies is more than doubled.)

For certain high-income taxpayers – single filers with adjusted gross income (AGI) in excess of $1 million and joint filers with AGI in excess of $1.2 million – the tax benefit of the 12 percent threshold would be phased out at a rate of 6% of the amount by which AGI exceeds the threshold, resulting in additional tax liability for such taxpayers.

KPMG NOTE

Although the "Unified Framework for Fixing Our Broken Tax Code" released by the White House and House Republicans on September 27, 2017 indicated an intention to have only three brackets (12, 25 and 35 percent), it indicated that an additional top rate could be retained for the highest income taxpayers.[2] The TCJA would retain the highest tax bracket but significantly increase the threshold at which it applies, to $1 million from its 2017 threshold of $470,700 for married taxpayers filing jointly, and to $500,000 from its 2017 threshold of $418,400 for single taxpayers.

Capital Gains and Investment Income

The TCJA would keep in place the current system whereby net capital gains and qualified dividends are generally subject to tax at a minimum rate of 20% or 15%, with higher rates for gains from collectibles and unrecaptured depreciation. The proposal retains the same "breakpoints" for application of these rates as under current law, except the breakpoints would be adjusted for inflation after 2017. For 2018, the 15% breakpoint would be $77,200 for married taxpayers filing jointly and $38,600 for single taxpayers. The 20% breakpoint would be $479,000 for joint returns, and $425,800 for single taxpayers.

The TCJA also would leave in place the current 3.8% net investment income tax.

Standard Deduction and Personal Exemptions

The TCJA would increase the standard deduction from its 2017 amount of $12,700 to $24,000 for married couples filing jointly and surviving spouses, and from $6,350 to $12,000 for unmarried individuals. Single filers with at least one qualifying child in the household could claim a standard deduction of $18,000.

Personal exemptions for taxpayers and dependents (currently $4,050 each for 2017) would be repealed.

Deductions

The TCJA would eliminate many deductions, including the deduction for state and local income and sales taxes, personal casualty losses, wagering losses, tax preparation expenses, medical expenses, alimony payments, moving expenses, contributions to medical savings accounts, and employee business expenses.

The deduction for state and local property taxes would be retained but would be capped at $10,000. Foreign real property taxes other than those incurred in a trade or business would not be deductible.

KPMG NOTE

Since foreign real property taxes are no longer deductible, this could increase assignment costs. A foreign national on a long-term assignment in the United States has previously been allowed a deduction for property taxes paid on a foreign residence. Under the proposal, this deduction is no longer allowed. If the individual is on a tax equalized program and the company is paying all the U.S. (host country) taxes, this will increase the cost of the assignment to the employer.

Moving Expense Reimbursement

The TCJA would repeal the exclusion for qualified moving expense reimbursements. Under current law, qualified moving expense reimbursements provided by an employer to an employee are excluded from the employee's income.

KPMG NOTE

The repeal of the above-the-line deduction for moving expenses as well as the repeal of the exclusion for qualified moving expense reimbursements would have a significant impact on the costs of sending employees on international assignment. Currently, employers are allowed to exclude many reimbursed costs of moving an employee overseas from the employee's income. Under the proposed law, the moving expenses would now be taxable, leaving the employer to pay potentially both home and host country taxes on that income.

Charitable Contributions

The deduction for charitable contributions would be largely retained in its current form, but the rule whereby a deduction for cash contributions to a public charity are limited to 50 percent of a taxpayer's AGI would be amended to increase the limit to 60 percent.

Deduction for Mortgage Interest

The deduction for mortgage interest would be retained for existing mortgage borrowers, subject to the current limitation on interest deductions for up to $1,000,000 of qualifying acquisition indebtedness. However, this limitation would be reduced to $500,000 of debt for mortgages taken out after November 2, 2017. For refinancings of mortgages incurred before this date, the refinanced debt would be treated as incurred on the same date as the original debt.
In addition, beginning in tax year 2018 mortgage interest would be deductible only if the loan proceeds are used to acquire, construct or substantially improve a qualifying residence; the separate deduction for home equity indebtedness would be repealed.

Finally, mortgage interest would only be deductible in relation to the taxpayer's principal residence, thus repealing the current rule whereby interest on a loan secured by a second home can also be deducted.

Exclusion of Gain from Sale of Principal Residence

The TCJA would amend the exclusion for gain from sale of a principal residence by increasing the period for which the taxpayer must have owned and used the property as a principal residence from two of the previous five years to five of the previous eight years. Also, the exclusion could be claimed only once every five years and would be subject to phase-out for taxpayers whose average modified AGI for the current and two prior years is in excess of $500,000 ($250,000 for single filers).

KPMG NOTE

The changes to the exclusion of gain from the sale of a principal residence could have significant implications on tax equalization calculations. For example, taxpayers on international assignment often have additional items of compensation which increase their AGI. The proposed changes add a phase-out to the exclusion which would mean that a taxpayer whose AGI has been increased due to assignment allowances may now not be able to take advantage of the home sale exclusion or his or her benefit could be reduced. If the taxpayer is part of a tax equalization program, the company would bear the burden of "equalizing" this and paying the difference. Also, the longer home use requirement (increased from 2 to 5 years) may make employees less mobile.

Exclusion for Employer-Provided Housing

The exclusion for housing and meals provided to employees and their spouses and dependents when provided for the convenience of the employer, which includes "camp housing", would be limited by the TCJA to $50,000 per year ($25,000 for married individuals filing separately) and would be subject to phase-out for taxpayers who meet the current definition of "highly compensated employees" (generally those with wages in excess of $120,000, adjusted annually for inflation). The exclusion would also be limited to one residence.

KPMG NOTE

The limitation on the exclusion for camp housing could have the effect of increasing taxable income for employees working at remote foreign locations where they are currently permitted to exclude all housing costs.

Alternative Minimum Tax

The TCJA would repeal the alternative minimum tax (AMT).

Contributions to Retirement Plans

Despite some speculation that the excludible amount for contributions to section 401(k) plans could be reduced, the TCJA would retain this at its current level ($18,000 for 2017, increasing to $18,500 for 2018, plus $6,000 for individuals aged 50 or older).

Child Tax Credit

The TCJA would significantly increase the child tax credit from $1,000 to $1,600. In addition, a credit of up to $300 could be claimed for dependents other than children. Also, a "family flexibility credit" of $300 could be claimed by a taxpayer (and the taxpayer's spouse if they file jointly).

The refundable portion of this credit would remain $1,000 as under current law, but would be increased annually pursuant to inflation adjustment. The income levels at which these credits are subject to phase-out would increase from $110,000 to $230,000 for joint filers, and from $75,000 to $115,000 for single filers.

The family flexibility credit and the non-child dependent credit would only be effective for tax years ending before 2023.

Estate Tax

The TCJA would increase the estate tax exemption from its current level of $5.49 million to $10.98 million. The estate tax and generation-skipping transfer tax would be repealed entirely for individuals who die after December 31, 2023.

Examples

Example 1

Neil is married and has 2 young children. His financial data is as follows:

Wages	Dividend Income	Qualified moving expenses	State income tax paid	Property Tax	Mortgage Interest	Charitable contributions
150,000	5,000	10,000	10,000	8,000	10,000	2,000

Under current law, Neil's 2018 income tax liability would be $15,158. Under the TCJA his 2018 tax liability would be $16,650.

Example 2

Same as Example 1, except that Neil exercised Incentive Stock Options, resulting in $100,000 of income that would be subject to Alternative Minimum Tax. The ISO exercise would increase his 2018 tax to $41,847 under current law, while under the TCJA his 2018 tax liability would remain $16,650.

Example 3

Buzz is married and has 4 children. His wages are $100,000, and he does not itemize his deductions. Under current law, Buzz's 2018 income tax liability would be $4,363. Under the TCJA, it would drop to $2,072.

Example 4

Sally is married and is nearing retirement age. Her children are grown. Her financial data is as follows:

Wages	Dividends and capital gains	Property Tax	Mortgage Interest	Charitable contributions
700,000	20,000	18,000	20,000	5,000

Under currently law, Sally's 2018 income tax liability would be $213,068. Under the TCJA, her 2018 tax liability would be $199,050.

Example 5

Same as Example 4, except that Sally and her spouse sold their home of the past 10 years at a gain of $500,000. Their average adjusted gross income for the most recent three years was $700,000. Under current law, her tax would remain the same, but due to her high level of income, under the TCJA the gain on her home would be partially taxable, resulting in a 2018 tax liability of $239,050.

Next Steps: An Uncertain Timeline with Many Political and Procedural Hurdles

It is anticipated that the House Ways and Means Committee will begin acting on the bill on November 6 and Chairman Brady expects passage out of the House the week of November 13. The Senate Finance Committee has yet to release its version of a tax reform bill, although it is anticipated on November 7, and Senate Republicans hope to have the bill pass the week of Thanksgiving. The legislative process is fluid so the timing may change, but KPMG LLP will endeavor to keep Flash Alert readers informed of subsequent developments as they occur.

FOOTNOTES:

1 See the text of the bill, H.R. 1, "Tax Cuts and Jobs Act."

For the announcement of the bill on the House of Representatives' Committee on Ways and Means website.

2 For discussion of the Unified Framework document, see GMS *Flash Alert* 2017-143, September, 28, 2017.

* * * *

Join KPMG LLP's Global Mobility Services for a webinar December 12, 2017

KPMG LLP's Global Mobility Services will be hosting a webinar on December 12, 2017 at 2 pm EST to discuss tax reform and global mobility policy considerations. Registration will open soon, so look for the registration link on our Global Mobility homepage at www.kpmg.com/us/globalmobility.

The above information is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230 as the content of this document is issued for general informational purposes only.

The information contained in this newsletter was submitted by the KPMG International member firm in the United States.

www.kpmg.com

kpmg.com/socialmedia

Flash Alert is a GMS publication of KPMG LLP's Washington National Tax practice. To view this publication or recent prior issues online, please click here. To learn more about our GMS practice, please visit us on the Internet: click here or go to http://www.kpmg.com.