**United States: New framework for tax reform released – rates are lower, but uncertainty looms for highest-income taxpayers**

October 2017

**In brief**

A nine-page ‘unified framework for fixing our broken tax code’ (the Framework) was released by the Trump Administration and Congressional Republican leaders on September 27, 2017. The Framework is the latest product of a tax reform working group known as the ‘Big 6’, which includes Treasury Secretary Steven Mnuchin and various other White House and Congressional members.

The Framework lowers individual tax rates – it proposes to replace the current seven federal individual tax brackets with three brackets, with rates set at 12%, 25%, and 35%. The new Framework, however, leaves open the possibility of a fourth tax bracket for highest-income individuals to meet President Trump’s goal of ensuring that tax reform “tremendously” benefits the middle class and not “the wealthy.”

Under the proposed Framework, the alternative minimum tax (AMT) regime for individuals would be repealed. The standard deduction would be doubled but the personal and dependent exemptions would be repealed. The plan would repeal ‘most itemized deductions’ except for mortgage interest and charitable donations, and tax incentives for work, higher education, and retirement security also would be retained.

Proposed changes under the Framework would impact multinational companies with globally mobile employees – those with US citizens and residents working abroad, and those with foreign nationals working in the United States. Employers that have adopted a tax-equalization or protection arrangement should review how these potential tax law changes could impact their tax reimbursement liabilities and gross-up costs for mobile employee populations.

There may be an immediate tendency to conclude that because US federal individual income tax rates generally could be reduced, US federal income tax costs will go down; however, this may not be the case for many individuals. More details are needed and companies should consider that the US federal income tax liabilities of some workers and executives may, in fact, increase. As more information becomes available, companies may want to consider possible changes to tax reimbursement policies, taking into account that tax law changes, if enacted, may not become effective until January 1, 2018.
**In detail**

*Comparison of the Framework to current law*

**Tax rates, standard deduction, and personal exemption**

<table>
<thead>
<tr>
<th>Framework</th>
<th>Current law for tax year 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Three individual income tax brackets: 12%, 25%, and 35%, but with a potential fourth bracket (additional top rate) for the highest-income taxpayers. The current standard deduction would be roughly doubled to $24,000 of income earned by a married couple filing jointly and $12,000 earned by a single individual, while current-law personal exemptions would be eliminated. The Framework proposals aim to stop the tax burden shifting from high-income to lower and middle income taxpayers. In addition, the Framework envisions ‘a more accurate measure of inflation for purposes of indexing the tax brackets and other tax parameters.’</td>
<td>Seven brackets – ranging from 10% to 39.6%. Standard deduction for married filing jointly is $12,700; $6,350 for single filers; $6,350 for married filing separately; $9,350 for head of household. The personal exemption amount is $4,050.</td>
</tr>
</tbody>
</table>

**Investment income**

<table>
<thead>
<tr>
<th>Framework</th>
<th>Current law for tax year 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Silent on issue of potential changes to investment tax rates.</td>
<td>Top statutory rate of 20% for long-term capital gains and qualified dividends and 39.6% for most other investment income; under current law, such tax liabilities can be increased by the 3.8% net investment income tax and the so-called Pease limitation on itemized deductions.</td>
</tr>
</tbody>
</table>

**Itemized deductions**

<table>
<thead>
<tr>
<th>Framework</th>
<th>Current law for tax year 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>‘Most itemized deductions’ are eliminated, except for tax incentives for home mortgage interest and charitable contributions. Tax incentives for work, higher education, and retirement security are also retained. The Framework infers that the federal deduction for state and local taxes will be eliminated (although not expressly stated.) No cap on itemized deductions is mentioned.</td>
<td>Many itemized deductions are allowed including home mortgage interest, charitable deductions, state and local taxes, and certain medical expenses. There is a reduction of itemized deductions by 3% of AGI in excess of: $261,500 (single); $313,800 (married filing jointly); $156,900 (married filing separate); $287,650 (head of household.)</td>
</tr>
</tbody>
</table>

**Child tax credit**

<table>
<thead>
<tr>
<th>Framework</th>
<th>Current law for tax year 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>‘Significant’ (but unspecified) increase to the child tax credit. Income levels at which the credit begins to phase out will be increased. The first $1,000 of the credit will be refundable. Also, a new $500 credit for non-child dependents will be introduced.</td>
<td>The child tax credit is currently $1,000. This amount is refundable. However, there is a phase-out of the credit for individuals with income over a certain amount.</td>
</tr>
</tbody>
</table>
AMT, estate tax, and generation-skipping transfer tax

Framework

AMT, estate tax, and generation-skipping transfer tax will be repealed.

Current law for tax year 2017

The current AMT regime creates significant complexity for individual taxpayers. Estate tax and generation-skipping transfer taxes apply.

* The above summary provides highlights only and is not an exhaustive list of proposed changes. The Framework states that additional changes will be introduced in the future, including measures to ‘reduce the tax burden on the middle class’, as well as to make the tax system ‘simpler and fairer for all families and individuals, and allow for lower tax rates.’

See previously released Global Mobility Insight on proposed tax reform.

Possible impact on tax reimbursement costs

These proposed changes are significant and, if enacted, will likely impact multinational companies with globally mobile employees. This would include both inbound and outbound employees, i.e., those US citizens and residents working abroad, and those foreign national employees working in the United States.

Many companies utilize so-called tax equalization arrangements for their employees and must properly budget and account for tax equalization expense. In such an arrangement, the employer assumes the employee’s obligation for actual taxes in exchange for the employee funding a so-called ‘hypothetical tax’. A year-end true-up is completed to reconcile the estimated hypothetical tax amount to a final hypothetical tax amount.

Will US federal tax liability increase or decrease?

Companies should consider how the proposals could impact the actual or hypothetical US federal income tax liabilities for mobile employees. For many employees, their US tax liabilities would be reduced. However, reduction should not be assumed across the board.

A critical issue will be how the proposed three brackets compare to income thresholds under current law. The Framework is silent as to what income range is attributable to each of the three percentages, further supporting that companies should wait for further details to conclude whether US federal tax liabilities for their expat populations will increase or decrease.

Moreover, mobile individuals who itemize deductions also could experience an adverse tax impact notwithstanding that the standard deduction would increase significantly.

The takeaway

Outlook for enactment of tax reform

The Framework is viewed as a major milestone in efforts to enact the first major tax reform legislation since 1986. While it offers more specifics on key issues, the Framework leaves many difficult policy issues open, to be resolved by the US Congress. Significant political hurdles must also be overcome if tax reform is to be enacted.

It is unclear when tax reform might be enacted, however, it is possible that tax reform legislation signed into call in late 2017 or early 2018 could be made generally effective January 1, 2018. Some members of Congress have suggested that individual tax rate relief could be made retroactively effective back to January 1, 2017 but fiscal and political issues may make such action unlikely.

Practical steps for mobility programs

Companies with mobile employees working in the United States, or US citizens or residents working abroad, should quantify and evaluate how reduced individual income tax rates and other tax reform changes could impact resulting tax costs under their equalization policies. This analysis may require looking at specific individual facts and circumstances in order to recalculate hypothetical taxes and tax reimbursement costs. This should be done even where mobility costs are in the form of overhead allocated based on a fixed multiplier to projects.

Depending on the outcome of this analysis, and the final provisions and effective dates of tax reform legislation, mobility programs should consider reviewing and potentially revising tax equalization policies. The current tax equalization policy may have assumed certain variables that no longer might be appropriate for most assignees if lower rates are enacted.

Other resources

For a broader description of potential US tax reform (including corporate tax reform), see PwC’s Tax Insight.
Let’s talk

For a deeper discussion of how this might affect your business, please contact your regular Global Mobility Services engagement team or one of the following team members:

**Global Mobility Services – Hong Kong/China**

<table>
<thead>
<tr>
<th>Name</th>
<th>Contact Information</th>
</tr>
</thead>
</table>
| James Clemence, Asia Leader | +852 2289 1818  
james.clemence@hk.pwc.com | |
| Robert Keys        | +852 2289 1872  
robert.b.keys@hk.pwc.com | |
| Theresa Chan       | +852 2289 1887  
theresa.ky.chan@hk.pwc.com | |
| Berin Chan         | +852 2289 5504  
berin.db.chan@hk.pwc.com | |
| Jane Cheung        | +86 (21) 2323 3031  
jane.kc.cheung@cn.pwc.com | |
| Steven Lim         | +852 2289 3998  
steven.lim@hk.pwc.com | |