

Memorandum

To: Mark A. Murray –NBC NEWS

November 15, 2017

From: Maury Cartine

Subject: Trump 2005 Joint U.S. Individual Income Tax Return and HR-1

Facts:

We have been asked to review the first two pages of the 2005 Form 1040 for Donald Trump and Melania Knavs and analyze the impact of HR-1, The Jobs Cut and Tax Act, on that income tax return as if HR-1 was enacted into law for that taxable year. We have been provided with copies of these first two pages by NBC. We cannot verify if this is the same return actually filed by the taxpayers, but for purposes of our analysis, we have assumed that the copies are true and correct versions of pages 1 and 2.

In analyzing the impact of HR-1, we have also assumed that the reported status of Donald Trump as a billionaire is correct.

Assumptions:

The impact of HR-1 on a 2005 federal income tax return necessarily requires several assumptions with respect to the federal income tax law in effect in 2005 versus the post 2005 federal income tax law that will still be in effect after the assumed enactment of HR-1.

1. The beneficial long-term capital gain rate was generally only 15% in 2005, but is now generally 20% even after the assumed enactment of HR-1. For purposes of this analysis, the beneficial tax rate for long-term capital gains is 20%
2. Although the net investment income tax of 3.8% did not exist in 2005, it will remain in effect even after the assumed enactment of HR-1. For purposes of this analysis, the 3.8% net investment income tax is treated as applicable.
3. The standard deduction is not taken into account since it would have only a de minimis impact on the analysis.
4. Tax benefits available only to lower income taxpayers are not taken into account.

Results of Analysis:

We have analyzed pages 1 and 2 and describe in order of importance the impact of HR-1, The Jobs Cut and Tax Act, on the information reported on the 2005 U.S. individual income tax return described above. Our analysis required a number of factual assumptions due to the limited amount of information provided on pages 1 and 2 of the 2005 Form 1040.

1. Alternative Minimum Tax:

Under HR-1, the alternative minimum tax would be repealed. Line 45 of page two of Form 1040 reports an alternative minimum tax liability of \$31,261,179. Assuming the alternative minimum tax was repealed under HR-1, the taxpayers would not have paid \$31,261,179 of alternative minimum tax. As might be expected and as described in the Summary provided by the House Ways and Means Committee on Page 26, the alternative minimum tax is one of the most far reaching complexities of the current "Code" (the Internal Revenue Code). In 2001, the Joint Committee on Taxation concluded that the alternative minimum tax "no longer serves the purposes for which it was intended." See page 27 of the Summary.

Whether or not the House Ways and Means Committee or the Joint Committee on Taxation is correct, the repeal of the alternative minimum tax would result in an initial federal income tax savings of \$31,261,179.

The initial federal income tax savings would be reduced by the additional regular tax that would be imposed by reason of the repeal of the state and local tax deduction and other itemized deductions under HR-1. The 2005 Form 1040 reports itemized deductions of \$17,034,485 on page 2, Line 40. It is not possible to determine how much of the itemized deductions are attributable to the state and local tax deduction and other itemized deductions without access to Schedule A of Form 1040, Itemized Deductions, for 2005. However, it seems likely that a substantial amount of the itemized deductions would be attributable to non-deductible state and local tax and other non-deductible expenses. The higher long-term capital gain tax rate of 20% and the net investment income tax of 3.8% would also reduce the tax savings attributable to the repeal of the alternative minimum tax. The impact of the tax rates and the non-deductible itemized deductions under HR-1 are further analyzed in item 2 below.

It is impossible to determine the items that were added back to taxable income in 2005 for purposes of computing alternative minimum taxable income without access to Form 6251 of Form 1040 for 2005. There are many addbacks including a portion of a net operating loss carryover, incentive stock options, depletion, certain depreciation of assets, mining costs, research and experimental costs, etc. Certain addbacks for alternative minimum tax purposes can result in an alternative minimum tax credit in future years. Thus, it is possible that some portion of the initial federal income tax savings would have been realized in future taxable years as an alternative minimum tax credit even without repeal of the alternative minimum tax under HR-1 and may be refundable in future years after the assumed enactment of HR-1.

2. Regular Tax and Net Investment Income Tax Computation:

The federal income tax was recomputed for 2005 using the proposed tax rates under HR-1. However, two important assumptions were made in computing the total tax. First, it was assumed that all of the capital gains reported on Line 13 of page 1 of the 2005 Form 1040 were long-term capital gains subject to the more beneficial 20% regular tax rate. This assumption appears to be relatively reasonable since the regular tax reported on Line 44 of page 2 of Form

1040 was approximately equal to 16.5 percent of the capital gains reported on Line 13 of page 1 of Form 1040. As noted under the Assumptions above, the beneficial long-term capital gain tax rate in 2005 was 15% and the excess of 1.5% is probably attributable to a much smaller amount of capital gains not eligible for the 15% rate. Second, it was assumed that all itemized deductions were non-deductible under HR-1.

The regular tax and the net investment income tax on the 2005 taxable income, recomputed as described in the preceding paragraph, is approximately \$14,000,000. The recomputed federal income tax of \$14,000,000 exceeds the actual 2005 regular federal income tax of \$5,310,616 by \$8,689,384 and reduces the initial federal income tax savings attributable to repeal of the alternative minimum tax.

3. Maximum Tax Rate on Business Income of Individuals:

HR-1 includes a provision that limits the tax rate on “qualified business income” to 25%. This maximum tax rate can provide significant savings for an individual that is self-employed, a partner in a partnership, a member of a limited liability company treated as a partnership or a shareholder in an S corporation. The 2005 Form 1040 includes business income of \$42,395,804 on Line 12 and income from rental real estate, royalties, partnerships, S corporations, trusts, etc. of \$67,383,658 on Line 17 of page 1 of Form 1040. However, the 2005 Form 1040 also includes an item of other loss of \$103,201,242 on Line 21 of page 1 of Form 1040. The income and loss from these lines substantially offset each other and it is impossible to determine if any of this income would either be separately eligible or eligible on a combined basis for the beneficial reduced tax rate of 25% on qualified business income. A substantial amount of the income reported on lines 12 and 17 of page 1 of Form 1040 is apparently derived from self-employment income. This is evident from the deduction for self-employment tax reported on line 27 of page 1 of Form 1040. While the payment of substantial self-employment tax may be indicative of “qualified business income”, the information reported on pages 1 and 2 of the 2005 Form 1040 are not sufficient to permit any conclusions one way or the other.

4. Business Interest Expense Limitations:

There are significant limitations on the deductibility on business interest expense under HR-1. Generally, the proposed law limits business interest deductions to 30% of adjusted taxable income. Interest expense in excess of the limit is not deductible in that taxable year, but may be carried forward to the succeeding five taxable years. Real property trades or businesses are excluded from the application of the limitation. It is not possible to determine if the business interest expense limitation would apply to any of the business activities reported on page 1 of the 2005 Form 1040

5. Increased Expensing and Expansion of Section 179 Expensing:

HR-1 permits accelerated expensing of depreciable assets. It is not possible to determine if any of the business income reported on page 1 of the 2005 Form 1040 would be reduced by the

accelerated expensing of depreciable assets under HR-1. Generally, real property would not be eligible for accelerated expensing.

Conclusion

Based upon the information reported on the copies of pages 1 and 2 of the 2005 Form 1040 provided to us and the above analysis, it appears that under HR-1, the federal income tax liability of Donald Trump and Melanija Knavs would be reduced from \$36,571,795 to \$14,000,000, resulting in a potential federal income tax savings of \$22,571,795.

The conclusion above is limited by the information made available to us. No attempt was made to quantify the federal income tax savings, if any, which could result from application of the maximum tax rate on qualified business income since the information available is not sufficient to permit the computation of qualified business income.

Many other provisions of HR-1 could be applicable to the items of income and deduction reported on the 2005 Form 1040. It is impossible to determine if any other provisions of HR-1 would apply without a complete 2005 federal income tax return.

The federal income tax savings that would result under HR-1 is primarily attributable to the repeal of the alternative minimum tax. It is not possible to determine the items of tax preference that were required to be added back in computing the alternative minimum tax as reported on page 2, Line 45 of the 2005 Form 1040 without access to Form 6251. If this information were available, it is possible that the conclusion provided hereinabove would change.