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GOP tax plan could squeeze middle class

By Dan Haar

So you live in Connecticut, you own a nice house, have a pretty good job, maybe you voted for Trump or perhaps you can't stand him. Regardless, you're eager to see how much you'd save under the federal tax reform plan Republicans are set to roll out as soon as Thursday.

Not so fast.

It's true that even though much of the benefit will fall to business owners and wealthy people, there's enough political pressure to help the middle class. Still, there will be households that pay more, not less.

You could be one of them - especially if you have an upper-middle income, say about $90,000 to $175,000, not from a small business that you own or partnership; your property tax is high and you don't have business losses to offset your state income tax bill or a house full of children.

Sound familiar? There are a lot of such households in Fairfield County - more than in most places - and the 2017 tax reform might leave them with a surprise if it passes.

"I don't think it's going to be a pleasant surprise," said Russell L. Abrahms, a certified public accountant and principal of a small accounting firm in Fairfield.

Many will be pleasantly surprised, of course. As we wait for the numbers, there are some broad principles and a few details we can see coming. The game is to see whether the basic rate you pay for taxable income declines enough to offset the deductions and exemptions you're going to lose.

The seven income brackets, topping out at 39.6 percent, will be reduced to three or four. The original plan called for the top rate to fall to 35 percent but that's now in jeopardy. That would cut into the savings for the rich, as the income subject to that top rate in 2016 was $466,951 for joint filers and $415,051 for individuals.

Even if the basic rates for taxable income fall, what is taxable income? Currently, filers can deduct the full amount they paid in state income tax and local property taxes, along with exemptions based on the size of the household and a deduction for mortgage interest.

The sacred mortgage interest deduction and child exemptions appear safe. Personal exemptions could be on the block, however.

And those state and local taxes - known in the accounting trade as SALT -- are on the block as deductions, although it now appears that local property taxes could be safer than we thought last week. Losing SALT deductions would be bad for Connecticut, with its income tax as high as 6.99 percent, and of course, losing the property tax deduction could be a killer for some families.

“Does it mean that people won’t be able to afford the more expensive home?” Abrahms asked. “Maybe I can’t swing the $2,200 to $3,200 monthly payment and I have to come up with a lower offer or I have to come up with more cash.”

In one example he gave me, a Fairfield County family with two Wall Street earners pulled in $900,000 in 2016 and had $100,000 in deductions, bringing their federal tax to $260,000. They could lose $65,000 of those deductions in the reform. In another example, a two-earner family making $135,000 paid $11,500 - and could see that bill jump by $5,700 - probably not enough to offset a lower base rate.

Losing the property tax deduction could jolt the local real estate market, Abrahms said. “We’ve seen it in Bridgeport…when real estate taxes go up, you can see that prices go down and there’s less activity.”

Another likely change would treat so-called pass-through income from privately owned businesses and partnerships as a separate category, taxed at well under the top rate - probably 25 percent, according to Abrahms and Kathi Mettler, an accounting professor and coordinator of the graduate accounting program at Fairfield University.

Suddenly the IRS would have to regulate how much ordinary salary income a business owner would have to take, as compared with profits, which would be taxed less. That could be an administrative nightmare, prompting Mettler to ask, “Isn’t the whole point of tax reform to be simpler?”

But that change won’t directly help the professional, salary-earning, home-owning professionals who also drive nice cars.

“That might be the taxpayer in our area that gets hurt the most,” Mettler said.

That demographic also happens to be among the most likely to have voted Democratic, or at least not for Trump. Hmmmm.

Also on the block is the federal estate tax, which is oddly hated by many working-class conservatives who have no chance of ever paying it, with the first $11 million exempted for couples. That could be phased out over time - maybe.

If it all seems like a mad, secretive rush, that’s because it is. Rep. Jim Himes, D-4th District, made the point that the last major tax reform in 1986 had some 400 witnesses at hearings and other testimony.

“They’re having a hard time getting a proposal together, which just illustrates that this is really hard work,” Himes told me Wednesday. “They’re just trying to ram this thing through.”

There are so many moving parts and so few specifics, none scored by the Congressional Budget Office, that Mettler couldn’t say what paths make the most sense. “At this point in time, this is all so unstructured,” she said. “It’s way too soon to say what’s right or wrong.”