OVERVIEW

Biden Administration's Tax Plans

AMERICAN FAMILIES PLAN

On April 28, 2021, the Biden White House released a fact sheet describing the "American Families Plan," which seeks to raise $1.5 trillion in revenue from wealthy taxpayers to cover new subsidies for families and workers. The tax proposals in the American Families Plan are laid out below.

RAISE THE TOP PERSONAL INCOME-TAX RATE

Current Law The highest personal income tax rate is 37%, which was enacted as part of 2017's Tax Cuts and Jobs Act (TCJA). Pre-TCJA, the highest personal income tax was 39.6%.

Taxpayers falling within the current top rate of 37% in 2021:

- Single filers with taxable income over $523,600
- Joint filers with taxable income over $628,300
- Married couples filing separate (MFS) returns with taxable income over $314,150
- Head-of-household filers with taxable income over $523,600

Biden Administration Proposal The American Families Plan would reverse the TCJA's rate change and bring the top rate back up to 39.6%.

President Biden has said he will not raise taxes on anyone making less than $400,000 per year, so it is not clear (given the MFS current top-rate gate above) whether the proposal will raise rates for taxpayers who are married and filing separately earning between $314,150 and $400,000.

INCREASE CAPITAL-GAINS RATE FOR TAXPAYERS EARNING $1,000,000 OR MORE

Current Law Rates applicable to long-term capital gains, *i.e.*, gains from the sale of stocks, mutual funds, and other capital assets held for at least one year, are taxed at a 0%, 15%, or 20% rate, depending on the amount of the taxpayer's taxable income. The 20% rate applies to single filers with taxable income over $445,850, head-of-household filers with taxable income over $473,750, and married couples filing a joint return with taxable income over $501,600. Short-term capital gains are taxed at the same rate as ordinary taxable income.

Biden Administration Proposal Taxpayers with taxable income over $1,000,000 would pay tax at the ordinary income rate of 39.6% on their long-term capital gains, thus eliminating the reduction in tax for capital gains. This rate increase is almost double the current top rate on long-term capital gains.

Those taxpayers with over $1,000,000 in taxable income would also see an application of the 3.8% Medicare tax on net investment income (NII) in Section 1411, bringing the top rate for such taxpayers' long-term capital gains to 43.4%.

With the addition of state and local capital-gains taxes, taxpayers with over $1,000,000 in taxable income could be paying long-term capital-gains taxes at a combined rate of over 58%, depending on where they live.

ELIMINATE THE BASIS STEP-UP FOR INHERITED PROPERTY

Current Law Taxpayers receive a basis step-up to fair market value on stock, real estate, and other capital assets inherited from an estate. In essence, this basis step-up allows the imbedded increase in fair market value to avoid capital-gains tax.

Biden Administration Proposal Calls for the nullification of the basis step-up effects for gains of $1,000,000 or more ($2,000,000 or more for married couples filing a joint return).

The specifics for how this would be accomplished are not entirely clear, but it appears the property would carry a tax obligation in the amount of embedded gain at time of death, with the tax liability falling on the estate. A previous proposal to limit the stepped-up basis, the Sensible Taxation and Equity Promotion (STEP) Act of 2021, gave families up to 15 years to pay the taxes owed on certain assets.

Exceptions would be carved out for property donated to charity and certain family-owned businesses and farms that heirs continue to operate.

ELIMINATE CARRIED-INTEREST ELIGIBILITY FOR LONG-TERM CAPITAL-GAINS RATES

Current Law Under certain circumstances, an investment fund manager can treat "carried interest," which is essentially earned income from fund management, as long-term capital gain. This treatment allows the income to be taxed at long-term capital-gains rates, which are currently considerably lower than ordinary income rates.

Biden Administration Proposal Eliminate the carried-interest rules. If the fund manager's taxable income is over the threshold for the top income tax rate, the tax on the fund manager's carried-interest income could go from a rate of 23.8% (20% capital gain rate + 3.8% surtax on NII) to 43.4% (39.6% ordinary tax rate + 3.8% surtax on NII).

LIMIT AVAILABILITY OF LIKE-KIND (SECTION 1031) EXCHANGE TREATMENT

Current Law Tax gain or loss can be deferred on exchanges of real property used for business or held as an investment for "like-kind" property. Properties are of like kind if they are of the same character. This is the case regardless of whether the properties differ in size or value.

Biden Administration Proposal Eliminate like-kind exchange treatment for gains greater than $500,000. This change would apply regardless of a taxpayer's taxable income.

MAKE BUSINESS LOSS-LIMITATION RULE PERMANENT

Current Law Under the TCJA (Section 461(l)), individuals operating a trade or business and filing a Schedule C cannot deduct losses in excess of $250,000 ($500,000 for joint filers). Excess losses may be carried forward to future tax years. This loss-limitation rule is currently set to expire in 2027.

Biden Administration Proposal Make permanent the business loss-limitation rule.

INCREASE IRS'S ENFORCEMENT BUDGET BY $80 BILLION OVER THE NEXT 10 YEARS

Biden Administration Proposal "[I]ncrease investment in the IRS, while ensuring that the additional resources go toward enforcement against those with the highest incomes, rather than Americans with actual income less than $400,000." The IRS would also focus resources on large corporations, other businesses, and estates.

To assist in these enforcement efforts, the plan calls for financial institutions to "report information on account flows so that earnings from investments and business activity are subject to reporting more like wages already are." The specifics of the reporting requirements are apparently not yet developed, but presumably the purpose is to identify unreported taxable income. The American Families Plan suggests that these increased tax-enforcement efforts would raise $700 billion in tax revenue over a 10-year period.

AMERICAN JOBS PLAN

On March 31, 2021, the Biden White House released a fact sheet describing the "American Jobs Plan," which contains a $2.3 trillion proposal for infrastructure spending that also contains certain tax credits outlined below.

TAX CREDIT PROPOSALS

- Point of sale rebates and tax incentives to buy American-made electric vehicles.
- Tax credits for low- and middle-income families and small businesses to invest in disaster resilience.
- Targeted investment tax credit for construction of at least 20 gigawatts of high-voltage capacity power lines.
- Extension and expansion of direct-pay investment tax credit and production tax credit for clean energy generation and clean energy storage.
- Reform and expansion of section 45Q tax credit, which provides a tax credit on a per-ton basis for CO2 that is sequestered by new equipment placed into service. Proposal to make the credit direct-pay and easier to use for certain industrial applications, air recapture, and retrofits of existing power plants.
- Targeted tax credits to expand affordable housing rental opportunities in underserved communities.
- Passage of the Neighborhood Homes Investment Act, which includes tax credits (proposed to be $20 billion over five years) to build or rehabilitate 500,000 homes.
- Expansion of home and commercial efficiency tax credits under the Weatherization Assistance Program.
- Expansion of tax credits (50% of the first $1 million in construction costs per facility) to encourage the building of childcare facilities at places of work.
- Extension of the section 48C tax-credit program, which would be aimed to build-out U.S. manufacturing capacity to supply clean energy projects with American-made parts and equipment.

MADE IN AMERICA TAX PLAN

On March 31, 2021, the Biden White House released a fact sheet describing the "Made in America Tax Plan," which is a tax proposal that would generate revenue for the American Jobs Plan spending. It is estimated that the Made in America Tax Plan will raise $2 trillion in tax revenue over the next 15 years. The Made in American Tax Plan proposals are laid out below.

RAISE CORPORATE INCOME TAX RATE

Current Law The TCJA lowered the corporate income tax rate to 21% for tax years beginning on or after January 1, 2018. From 1994–2017, the top effective corporate income tax rate was 35%.

Biden Administration Proposal Increase the corporate income tax rate to 28%.

RAISE TAX RATE ON GILTI

Current Law *Background:* The TCJA identified a new type of income, Global Intangible Low-Taxed Income (GILTI), which is an approximation of a taxpayer's (a U.S. shareholder) allocable share of amounts earned by a controlled foreign corporations (CFC) outside the U.S. in excess of routine returns on tangible property.

A deduction equal to 50% of its GILTI inclusions is afforded taxpayers to achieve an effective tax rate on GILTI of 10.5% (13.125% in tax years after 2025, achieved by reducing the deduction to 37.5% of GILTI inclusions).

The tax on GILTI inclusions may be reduced by 80% of any foreign tax credits (FTCs) for foreign income taxes imposed on the foreign earnings. A CFC's U.S. shareholder (the taxpayer) with GILTI subject to 13.125% foreign income tax would be allowed 80% of those foreign income taxes as FTCs. The 13.125% of FTCs would entirely offset the 10.5% federal income tax on GILTI inclusions.

Biden Administration Proposal Raise the effective GILTI federal tax rate to 21%. The rate increase is achieved by reducing the GILTI deduction to 25% of a U.S. shareholder's GILTI inclusions.

For a taxpayer to have a full offset of the 21% federal income tax on its GILTI inclusions from FTCs, its CFC(s) would need to have GILTI subject to 26.25% foreign income tax.

ELIMINATE THE QBAI EXEMPTION FOR GILTI

Current Law In calculating its GILTI, a taxpayer is allowed a reduction in GILTI inclusions by an imputed return of 10% on its foreign subsidiaries' depreciable tangible assets (qualified business asset investment or QBAI).

Biden Administration Proposal Repeal the QBAI exemption. The repeal of the QBAI exemption would have the result of increasing a taxpayer's GILTI inclusions.

REQUIRE COUNTRY-BY-COUNTRY GILTI CALCULATION

Current Law GILTI is determined on a blended-country basis. This method has been criticized by the Biden administration, as well as academics, as allowing a taxpayer to avoid the GILTI tax with respect to its CFCs operating in low tax-rate countries by "blending" the low rate with income from CFCs operating in high tax-rate countries.

Biden Administration Proposal Require GILTI be determined on a country-by-country basis. Effectively, eliminating the tax rate blending concern/approach.

REPEALING THE FDII DEDUCTION

Current Law *Background:* As a "carrot" to the "stick" that is the tax on GILTI, the TCJA enacted a deduction to reduce the effective federal income tax rate for a domestic corporate taxpayer's Foreign-Derived Intangible Income (FDII). Examples of FDII include income from export sales and licensing royalties paid by foreign entities.

Taxpayers are permitted a deduction of 37.5% of their FDII to achieve an effective tax rate of 13.125% (16.406% for tax years beginning in 2026, achieved by reducing the deduction to 21.875% of FDII).

Biden Administration Proposal Repeal the FDII deduction. The Biden administration has labeled the FDII deduction as giving "corporations a tax break for shifting assets abroad and is ineffective at encouraging corporations to invest in R&D."

REPEAL AND REPLACEMENT OF BEAT

Current Law The TCJA enacted the Base Erosion Anti-Abuse Tax (BEAT), which generally imposes a 10% minimum tax (5% in 2018) on a taxpayer's income determined without regard to tax deductions arising from base erosion payments (including the portions of a taxpayer's net operating loss (NOL) deduction treated as related to base erosion payments), which generally cannot be reduced by credits other than, through 2025, the research credit under section 41(a) and 80% of other credits.

Biden Administration Proposal Replacing BEAT with the Stopping Harmful Inversions and Ending Low-tax Developments (SHIELD), which would deny tax deductions by reference to payments made by taxpayers to related parties that are subject to a "low effective rate of tax." The low effective rate of tax is yet to be determined, but Treasury has announced that until such announcement, "the default rate trigger would be the tax rate on the GILTI income [sic], as modified by the [Made in America Tax] plan."

MINIMUM CORPORATE TAX ON "BOOK INCOME"

Biden Administration Proposal Impose a 15% minimum tax on "large, profitable corporations" based on "book income." For this purpose, book income appears to refer to GAAP income.

STRENGTHENING ANTI-INVERSION RULES

Biden Administration Proposal Initiative to prevent U.S. corporations from merging with foreign corporations and reducing their federal income tax (by replacing the U.S. parent with a foreign parent, with the U.S. parent becoming a subsidiary of the foreign parent, thereby moving its tax residence to such foreign country) while retaining management and operations in the U.S.

AMERICAN RESCUE PLAN

On March 11, 2021, President Biden signed into law the "American Rescue Plan Act," a $1.9 trillion legislation containing, among other provisions, $1,400 Economic Impact Payments to qualifying US taxpayers. The tax aspects of the American Rescue Plan Act are laid out below.

- For 2021, the child tax credit is $3,600 per child under the age of 6 and $3,000 per child that is 6 through 17 years old, which is fully refundable and payable in advance. The credit revers to $2,000 per child under the age of 17 for 2022.
- For 2021, the maximum child and independent care tax credit for one individual is $4,000 and $8,000 for two or more qualifying individuals. The credit is refundable for some taxpayers.
- Extension of the earned income credit (EITC) to workers under age 25. Individuals as young as age 19 are eligible for 2021, as well as being entitled to apply the credit to more earned income with the added benefit of a higher phase-out level. There is no longer a maximum age for eligibility.
- Premium reductions for Affordable Care Act (ACA) health insurance coverage through the application of premium tax credits effective for two years.

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